THE INDIAN ECONOMY

ITS GROWTH AND PROBLEMS

With a Foreword

BY

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Foreword

Ever since we wrote that book, An Introduction to Economic Theory, it has been the ambition of the Publishers to print "An Introduction" series, covering a number of books on social sciences. The intervention of the war, the Partition of the country and the subsequent unsettled conditions stood in the way of the realisation of that ambition. At last talks about the Five Year Plans reminded them of their own plan, and they succeeded in inducing Prof. Das and Prof. Chatterji to undertake the task of writing the present book on Indian Economics. As one of the writers of the first book of this series, it has fallen to me to write a foreword, introducing this new "introduction" to the reading public and the students.

I have read the manuscript and have been struck by the preseverance and the competence with which the authors have marshalled their facts. Indian economy is now on the march, and a number of Surveys and Committees are busy throwing light on the hitherto unknown or little known sectors of the economic organisation. Profs. Das and Chatterji have striven hard to gather all this information and to present them in a simple lucid style for the busy readers of the subject.

As I have told the authors, there are portions which some people may find it difficult to accept. There are also places where I would have liked them to pursue the analysis further to its logical conclusion. On the whole I have nothing but praise for the efficient manner in which these two authors have carried out the task they have set out before themselves.

S. N. SEN.

PREFACE TO THE TENTH EDITION

We have taken advantage of the occasion to revise the text extensively and to bring all topics as uptodate as is possible with our data. The new levies imposed by T.T.K. have been analysed in appropriate places, and at the end we have added a note on the progress of the Third Five-year Plan and an outline of the Draft Fourth Plan. Throughout we have made an attempt to present an analytical account of the march of the Indian economy in its various aspects, carefully noting in different places the impact of the great and bold experiment in planning through democratic means in which this country is now engaged.

2nd May, 1967 DAS & CHATTERJI

PREFACE TO THE FIRST EDITION

This book has been written in answer to a large number of requests that we received from our students to publish our lectures. We also felt the need of an up-to-date book on Indian Economics, which was neither too large for the average reader, nor too small to be intelligible. We have tried to focus attention on the main problems in every sphere of the economic life of this country and to give a broad analysis of their implications. It has been our aim to maintain a proper balance between the different parts of the subject. avoiding too much elaboration of the earlier topics, and too little discussion in the later chapters.

We offer our heartfelt thanks to our teacher, Dr. S. N. Sen, of the Department of Economics, University of Calcutta, who so kindly agreed to read the manuscript and to write a foreword, in spite of his so many engagements. The book has no doubt been improved in many places as a result of his valuable suggestions. It must, however, be understood that he is not responsible for the opinion expressed in this book or for its defects and mistakes.

We also thank our Printers, the Basusree Press, and the Publishers whose co-operation has made it possible for us to print this book within a short time. Our desire to publish the book hurriedly has unfortunately been responsible for a number of printing mistakes for which we crave the indulgence of our readers.

DAS & CHATTERJI

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CHAPTER 1

CHARACTERISTICS OF THE INDIAN ECONOMY

Is India under-developed? India is commonly regarded as an under-developed country with a large and rapidly growing population. What are the usual characteristics of an under-developed country, and how far are they present in the case of India? At first sight it appears quite reasonable to assume that a country whose resources have not been fully developed is to be regarded as under-developed. But in that sense even the most developed countries like the USA or the UK can be regarded as under-developed as it cannot be said that all their resources have been fully developed. There will always be some unutilised or under-developed resources even in a highly developed country. All that one can assume is that the extent of under-development is considerably large in the case of India than that in the USA or the UK.

The most usual test of an under-developed country is the amount of its per capita income. A country with developed resources will usually be a richer country than another with under-developed resources. Let us, therefore, analyse the per capita incomes in different countries. The per capita income was only Rs. 327 per year (at current prices) in India in 1960-61. This is to be compared with the per capita income of Rs. 10708 in the USA (1959), Rs. 4351 in the U.K. (1959), Rs. 7621 in Canada (1959), and Rs. 4128 in W. Germany (1959). Among the Asian countries the per capita income was much higher in Japan (Rs. 1425 in 1959), and in Ceylon (Rs. 560 in 1959) than it was in India. This shows that, as compared to these countries, India is under-developed as her per capita income is one of the lowest in the world. One may draw a line somewhere and say that all countries with per capita incomes below this level are to be regarded as under-developed.

A low per capita income is no doubt an important indicator of under-development. But a country may be extremely poor in natural resources, and if these small resources are fully developed, the total income may still be very small, and its per capita income may be low. Such a country cannot be regarded as under-developed, even though its per capita income is low. In order to come to a definite conclusion, it is, therefore, necessary to examine the question whether

the resources of the country are large or small in relation to its size of its population and the stage or method of development of these resources, in addition to the level of the per capita income of the country.

Sometimes other tests have been suggested for determining the state of development of a country such as the relative importance of agriculture and industry in the economic organisation, the occupational distribution of the population etc. A developed country is generally a highly industrialised country, where agriculture occupies a comparatively less important place. The larger part of the national income of the country is derived from manufacturing industries. In India, on the other hand, about 48 to 50 p.c. of the total national income is derived from agricultural and allied pursuits, whereas the income from large-scale industry, mining and small industries amounts to only 18 p.c. of the national income. This is also reflected in the occupational distribution of population. In a developed country, a comparatively smaller proportion of the population is dependent on agriculture, whereas in India about 68 p.c. of the population is dependent on agriculture. Moreover, an under-developed country will have a small number of industries, *i.e.* small as compared to its resources. As it is less industrialised, it will also be less urbanised. In other words, the vast majority of its population would be found to be living in the villages rather than in the cities and towns. In India, less than 18 p.c. of the total population live in the urban areas, which provides another evidence that its industrial development has not proceeded far.

The rate of growth of population, its birth rate and death rates, the average expectation of life,—these are sometimes regarded as providing some indication of the state of development reached by a country. It has generally been found that as a country grows richer through the development of its resources, its birth rate had declined and the rate of growth of population had slackened, and the average expectation of life had also risen significantly. Low birth and death rates, a slow rate of growth of population, a high average expectation of life,—these are all found together in the case of developed countries. An under-developed country has, on the other hand, high birth and death rates, a rapidly growing population and a low average expectation of life. All these features are to be found in the case of India.

India has thus all the usual features of an under-developed country :—a low per capita income with a large area, a large population

and comparatively large natural resources, a low proportion of income derived from manufacturing operations and a low proportion of the population engaged in industrial occupations, a low urbanised economy, with high birth and death rates, rapid growth of population and low average expectation of life etc. Thus it provides a typical illustration of an under-developed economy with a very large and rapidly growing population, but with very small capital resources.

The central problem of the Indian economy: The fundamental economic problem for India is how to raise the income of the people above its absurdly low level. As the rate of growth of population is not likely to slacken in the near future, the tempo of economic development has, therefore, to be kept at a sufficiently high level so that an appreciable increase in the standard of living of the people may be achieved in course of the next ten or fifteen years. The rate of growth of the national income must be faster than that of the population.

One outstanding characteristic of the Indian economy is the large preponderance of agriculture in the national economy. Nearly half the net national product of India is obtained from agriculture and allied activities. More than 82 per cent of the total population live in the rural areas, and about 68 per cent depend on agriculture as their principal means of livelihood compared to less than a third of the population in Europe. But unfortunately such an important sector of the economy has remained more or less stagnant with only a comparatively small increase in the total yield of agricultural crops or little change in the character of agriculture. As a result, India has now to depend on imports of foodgrains to feed its population, and on imports of jute and raw cotton for its important industries. It is only since the formulation of the First Five Year Plan in 1950-51 that greater attention is now being paid to introduce important changes in the agricultural economy. The extremely low agricultural productivity has meant very low incomes for the rural population. This factor, coupled with the well-known fluctuations in the prices of primary products, is responsible for introducing an element of serious instability into the general economy, and has proved to be a large stumbling-block to the task of developing other resources of the country.

The last fifteen years have brought about important changes in the industrial sector. A number of important industries like the cotton textile industry, sugar, iron and steel, paper, cement, soap etc. had already been established before 1947. As a result, the country has been able to reduce its dependence on foreign

sources of supply in most of these consumption goods. After the achievement of independence a large number of producers' goods industries have been set up. The industrial sector is fast growing into importance. But unfortunately, the occupational pattern of the population has shown only an insignificant change over the last two or three decades. And in spite of the industrialisation of the fifties, the ratio of urban population has remained more or less stagnant. Moreover, population is growing at rapid rates; agriculture has remained practically stagnant, and in the meantime, India's share in the world trade had been falling. These are important deficiencies and the combined result of all these factors has been the fact that over the two decades before 1950 there has been little increase in the over-all supply of goods and services available for domestic consumption. Some improvement has no doubt taken place during the fifties as a result of the large-scale investment expenditure under the two plans. The per capita income has risen over this decade by about 18·4 p.c., while the national income has increased by 43·4 p.c. in 10 years. But the pace of development has been rather slow, and even this has given rise to a number of stresses and strains.

Actually the rate of growth of the Indian economy during the last decade compares unfavourably with the rates of growth not only in the advanced countries but also in some of the other developing countries. The national product of Burma has increased by about 6 p.c. per annum, that of Ghana by 5 p.c., while Japan has achieved the highest growth rate (9 p.c.).

The result of all these facts has been the extremely low rate of saving in this country. In 1950-51, the first year of planning, net investment amounted to only 6·9 p.c. of the national income, which is much smaller than that in the developed economies, and is definitely less than what we need for the successful operation of the Five Year Plans. Even according to the most favourable estimates of the National Council of Applied Economic Research, the rate of savings increased to only 10 p.c. of the national income in the first two years of the Second Plan. Such a low rate of saving has meant a slow rate of economic development. The fundamental economic problem of India is how to generate a higher rate of saving in order that economic growth may proceed at a faster rate than that of the increase in population.

Plan of study: It will be the aim of this book to study this question from different aspects. We propose to start with an assessment of the aggregate economic resources available in this country. This will be followed by an

analysis of the implications of the growth of population and of the social framework in which the people live and work. A detailed study of the different aspects of the existing economic organisation such as agriculture, industry, transport, trade, the monetary system, public finance etc. will then be undertaken. Last of all, a review of the working of the Five Year Plans framed by the Planning Commission for raising the standard of living of the people and for solving the problem of unemployment and under-employment will be made. In each case, an attempt will be made to analyse the principal defects which are hampering our progress, with some suggestions, here and there, for the adoption of measures for the removal of these difficulties.

Questions

1. What are the tests by which you can decide whether a country is developed or under-developed ? Is India under-developed ?

2. Give a brief description of some of the prominent characteristics of the Indian economy. (Bom. 1951 ; Raj. 1953).

3. What, in your opinion, is the central problem of the Indian economy ? (I.A.S. 1951).

CHAPTER 2 PHYSICAL FEATURES

The first step in any realistic study of the economic conditions of a country is to know its physical features. These provide the background for the development of the resources of the country. The physical features of a country exercise a considerable influence over its economic organisation. Hence we propose to start our discussion with a study of the physical features of India.

A recent study has divided India into five natural divisions—the Himalayan Region, the Northern Plains Region, the Peninsular Hills and Plateau Region, the Western Ghats and Coastal Region and the Eastern Ghats and Coastal Region.

The Himalayan Region. The great Himalayan mountains stretch for 1500 miles between the Brahmaputra on the east and the gorges of the Indus on the west. It includes four divisions, the Jammu and Kashmir, the Himachal Pradesh, the Northern areas of Uttar Pradesh, West Bengal and the Assam Hill Division. This is a predominantly mountaneous region, varying in elevation from 200 ft. to 21,500 ft. This region is economically important as it contains large deposits of rock-salt, gypsum, coal, magnesite, dolomite, petroleum etc. It also grows a large variety of crops like tea, paddy, sugarcane etc. and different kinds of fruits. There are large areas of forests yielding a good supply of timber. This region includes some of the most well-known and delightful hill stations like Simla, Mussoorie, the valley of Srinagar, Darjeeling etc.

The Northern Plains Region consists of 4 division,—Uttar Pradesh except the eastern parts of the State, the lower Gangetic Plains (the whole of Bihar, West Bengal excepting the Himalayan districts and the eastern parts of U. P.) ; the Trans-Gangetic Plains (the plains of Punjab, Rajasthan, and the low-lying areas of Madhya Pradesh) ; and the Desert Division (West Rajasthan). This Region is traversed by two great river systems—the five western rivers comprising the Indus, the Ganges and the Brahmaputra. These rivers have formed rich, alluvial soils, which yield almost every kind of crops and vegetation.

The Peninsular Hills and Plateau Region comprises the south-eastern hilly areas of Rajasthan, the whole of the Madhya Bharat

Plateau, the U. P. Hills and Plateau, Choto Nagpur, some districts of Orissa, parts of Maharashtra, Deccan etc. The chief minerals of value are mica, iron ore, coal, manganese, copper etc. This is also well-known for a great variety of building stones like sandstones, limestones, marbles etc.

The Western Ghats and Coastal Region comprises the whole of Guzarat, Saurashtra, and Kutch, Kerala, Coorg in Mysore, etc. Salt obtained from the coastal areas of this Region forms nearly one-third of the total Indian production. The beach sands along the Travancore coast contain large reserves of ilmenite. It grows large quantities of rice, cotton, oilseeds, maize etc.

The Eastern Ghats and Coastal Region consists of North Madras and Orissa coast, and Southern Madras. It also grows a large variety of crops like rice, oil seeds, jowar, bajra, maize, gram etc. There are large deposits of magnesite, iron ore, limestone and bauxite etc.

Soils: Four main classes of soils are found extensively all over the country :—alluvial soils, black soils, laterite soils and red soils.

Alluvial Soils are found in U.P., Maharashtra, Deccan, Bihar, West Bengal, Orissa, parts of Madras etc. This soil contains varying amounts of salt and is extremely suitable for growing a large variety of crops.

Black Soils are generally suitable for the cultivation of cotton. These occupy greater part of Maharashtra and Saurashtra, western parts of Madhya Pradesh, Madhya Bharat, and some parts of Madras. These soils are generally deficient in nitrogen and other organic matter.

Red Soils comprise practically the major part of Madras, Mysore, south-east Maharashtra, greater part of the Santhal Parganas in Bihar, the Birbhum district in West Bengal etc. These soils differ in depth and variety and lack good cherical properties. They may, however, grow a large variety of crops with a good system of irrigation.

Laterite Soils are deficient in Potash, Phosphoric acid and lime They are to be found in certain parts of Orissa, Guzarat, Malabar in Kerala, Assam, Madhya Pradesh etc. They are not fertile.

The most common characteristic of these soils is their dryness. Hence it becomes necessary to carry out large projects of irrigation to supply water to these soils.

Climate: Owing to the great size and position of the country, there are many striking contrasts in climatic conditions in India. In the north-west lies the great Thor desert with an annual average rainfall of 5 inches. In the north-east the average annual rainfall is bout 425 inches at Cherrapunji in the Khasi Hills. There are places like Ganganagar in Rajasthan where the temperature rises over 120°F, while the minimum temperature falls as low as 40°F in Kashmir. There are also large variations in temperature, for example, in West Rajasthan the temperature goes up to 122°F in May and falls to 38°F in January. The result of such a diversity of climates is that India produces a great variety of animal, vegetable and mineral products, "from the wheat, fruit and fir-trees of the north to the rice and cocoanuts of the hot, lowlying swamps and coastal regions."

The Monsoons: Economically the most significant feature of the climate of India is the monsoons. The word, monsoons, is applied to the seasonal winds which change directions twice a year. These winds bring rainfall and that is why the arrival of the monsoons signifies the beginning of the rainy season. The causes of the monsoons are many and complex. But the fundamental cause is the periodic excess of heating of the land areas in summer and of cooling in winter as compared to the waters of the Indian ocean. The monsoons come in two currents ; the South-west monsoons and the North-east monsoons. The south-west monsoons generally blow during the months of June to September. This relatively cool and humid current bursts on the Malabar coast during the first five days of June and is usually established over most of the country by the end of June. It may be regarded as consisting of two currents,—the Bay of Bengal current and the Arabian Sea current. The former travels over the east coast of India, covers the whole of Bengal and Assam and is then deflected westwards up the Gangetic Plain. The Arabian Sea current covers the Western ghats and then advances over the Deccan and Madhya Pradesh. The total rainfall during this monsoon season is over 100 inches in the north Assam valley and parts of the west coast, and diminishes steadily until it is less than 5 inches in parts of Rajasthan. The north-east monsoons are of land origin and generally prevail during the months of December to February. From about the middle of December, the clear weather in northern India is broken at intervals by a series of disturbances which travel eastward. The amount of rainfall is comparatively small no doubt. But it is very important for the winter crops of north-west India.

One important characteristic of the monsoons is their great variability, both in time and space. The amount of rainfall varies in different parts of the country and also at different periods of time and year. The average annual rainfall in India is about 42 inches. There have, however, been years when the average rainfall increased to 54 inches and fell to 34 inches. It has often happened that in the same year some parts of the country are suffering from draught while other areas are sometimes deluged with rain and suffer distress through excessive flooding.

India has been classified into three areas according to the amount of rainfall :—(a) areas of good rainfall on the average, such as Assam and parts of West Bengal, (b) areas of precarious rainfall, such as Maharashtra, Deccan excluding the Western ghats etc. and (c) areas of draught, such as West Rajasthan.

Economic effects of the monsoons: The monsoons have influenced the economic life of India in many ways. India is primarily an agricultural country where about 68 p.c. of the total population depend upon agriculture for their livelihood. The soils of India are comparatively dry and do not grow large crops unless adequate quantities of water are applied to land. The supply of water to the thirsty land in due time and proportion is thus of paramount importance. If the commencement of rains is delayed over a large part of the country, or if there is a prolonged break or breaks in July or August, or if the rain terminates earlier than usual ;—all this is disastrous to the crops and produces draughts and famine. A shortage in the production of the more important agricultural crops affects the whole economy of the country. The vast majority of cultivators are so poor that if they have no or few crops to sell, they will suffer miserably. Their incomes fall and they will be unable to buy their usual requirements. As a result, our industries will also be hard hit. In the first place, the supply of industrial raw materials like raw jute, raw cotton, oilseeds etc., will decline and their prices will rise, while their main buyers, the cultivators, are no longer in a position to buy the products of industries at the same rate as before. On account of the smaller production of the raw materials and food crops, exports of raw materials will decline and most probably we may have to import raw materials and food-stuffs in larger quantities than before. As a result, the balance of trade will tend to move against the country. The operations of the various governments will also be seriously affected. The expenditure of the state and central governments will increase as they will have to spend money on the relief of the famine-stricken population. On the

other hand, their revenues will decline on various accounts. As the industries are depressed, the yield of income tax will fall. The railway revenues will decline as they carry smaller quantities of goods and passengers than they used to do in more prosperous years. Land revenue collections also fall off as the state governments will have to grant remissions of land revenue on account of the bad crops. Hence a failure of the monsoons is likely to turn even a surplus budget into a deficit one. That is why the budgets of the Governments of India have been called "as a gamble in rainfall". It is doubtful if any other single group of weather phenomena is so far-reaching in its effects.

The monsoons have also exercised some influence over other aspects of our economic organisation. They have, for example, affected the density of population in different parts of the country. Regions of abundant rainfall like West Bengal or Bihar have usually a very high density of population ; while places like West Rajasthan where rainfall is scanty contain the lowest density of population.

Questions

1. Give a brief survey of the different natural regions of India. To what extent are the production and trade of the different regions of India determined by geographical factors? (Punj. 1937 ; All. 1936).

2. Briefly describe the important varieties of soils in India, and point out their suitability for the growth of particular kinds of crops. (Cal. B. Com. 1941).

3. "Probably there is no other single group of weather phenomena which is so far-reaching to its effects, as the Indian monsoon." Discuss.

Describe the various economic consequences which follow from the failure of the monsoon. (C.U. 1937, 1936, 1934, 1931, 1930).

CHAPTER 3

NATURAL RESOURCES

The next step after a study of the physical features of a country is an examination of its natural resources. The latter determine to a large extent the total wealth of the community.

Our natural resources may be studied under the following heads :— mineral resources, power resources, agricultural resources, forests and fisheries.

Mineral resources: Mineral resources may be studied under three groups according to their commercial importance :—minerals which are important exports, minerals in which we are more or less self-supporting and minerals which must be imported. To the first group belong such minerals as mica, ilmenite, manganese, magnesite, iron ore etc. We are more or less self-sufficient in coal, bauxite, salt, graphite, barium etc. To the last group belong oil, copper, lead, zinc, tin, sulphur, asbestos, china clays, nickel, mercury etc. We propose to examine these in details.

Coal: The major portion of coal mines is concentrated in one enormous series of deposits known as the "Gondwana system". The principal workable coal deposits of the Gondwana system are to be found in West Bengal, Bihar, Orissa and Madhya Pradesh. The "tertiary" beds of coal are to be found in Assam, Punjab and Kashmir. The coal fields of West Bengal and Bihar produce more than 80 per cent of the total coal raised in India. Of the total coal produced in India, Bihar accounts for about 55 p.c., West Bengal for about 28 p.c., Madhya Pradesh for 6 p.c., Orissa 5 p.c., etc. This concentration of coal production in the eastern parts of the country is one of the most serious defects in our industrial organisation. As a consequence of this concentration, coal has to be transported by railways at considerable costs to other parts of India, and this raises the cost of production in other industries using coal.

A second problem in connection with the coal deposits is the comparative inadequacy of the reserves of good quality, metallurgical coal. It has been estimated that while the reserves of low grade coal are quite satisfactory, those of good quality coal are not adequate. According to the report of the Metallurgical Coal Conservation Committee of 1950, a reserve of 2,000 m. tons of such coal could be

obtained with the adoption of suitable measures of stowing, washing and blending. The Committee, however, warned that this figure may be halved unless proper precautions are taken in mining. Hence it has been suggested that proper steps should be taken to conserve the production of good quality coal and to restrict its use to metallurgical and other essential purposes. Recently a number of steps have been taken in this direction and the government has set up a Coal Board for adopting and carrying out measures of conservation of good quality coal.

There are about 1000 collieries in India and the total production has increased from an average of 30 m. tons in 1945-50 to 56·1 m. tons in 1961. The government proposes to increase the output of coal to 60 m. tons per year at the end of the Third Plan period.

Iron Ore: We possess vast deposits of iron ores which are to be found in Bihar, Orissa, Madhya Pradesh, Madras and Mysore. Most of these ores are also very rich in iron content, varying from 55 to 68 p.c. We are also fortunate in another fact that coal deposits are also situated near the iron ores in the eastern parts of the country. The reserves are estimated to be over 2100 crore tons. The iron and steel industry is one of the best organised industries of our country, and the value of the products of this industry amounted to Rs. 56·40 crores in 1950. The annual production of iron ore has amounted to 12·3 m. tons in 1961, and that of pig iron 5·6 m. tons and of steel 3·6 m. tons in 1961.

Manganese: India produces manganese ore of high quality. The principal deposits are to be found in Madhya Pradesh, Bihar, Orissa, Madras, Mysore, Bombay and Rajasthan. Reserves of high grade ores are estimated to be between 15 to 20 million tons. Manganese is one of the key metals and is used mainly in the manufacture of steel. The average production has been about 1·2 m. tons in 1961 out of which a little less than 1 m. tons are exported.

Mica: India is the largest producer of mica, producing nearly 75 p.c. of the world's output of block and sheet mica. The main regions of mica production are Bihar, Madras and Rajasthan. The mica belt in Hazaribag and Gaya districts of Bihar is the oldest and the most important. Mica is used mainly in the electrical and technical industries. Our annual production of crude mica was 28,000 tons in 1961. Most of our mica output is exported. The exports of mica have increased from Rs. 1·5 crores in 1940-41 to Rs. 10 crores in 1961.

Copper: In India, copper is mined in Singhbhum of Bihar. Small deposits have been found also in Assam, West Bengal, Madhya

Pradesh, Madras, Mysore, Rajasthan, Sikkim etc. But the majority of these are not of economic importance. India produces about 8,000 tons of copper whereas her annual requirement is about 26,000 tons. Imports of copper amounted to 26,997 tons in 1954-55.

Magnesite: India has excellent deposits of magnesite, to be found mainly in Madras and Mysore. This mineral is used for the manufacture of refractory bricks, special cement and in the chemical industry. The average annual production is about 1 lakh ton out of which about 46,000 tons are exported.

Ilmenite: India has now become the world's leading producer of ilmenite. It is the whitest of all substances and is used in the manufacture of white pigment. It is found in the 'Black sand' of the beaches near Travancore and the Cape Comorin. There is a large export trade in this mineral. We produce annually about 174,000 tons of ilmenite.

Monazite: It is produced as a by-product of ilmenite and is available on the beach sands of Travancore and Cape Comorin. India supplies about 88 p.c. of the world's requirement of this metal. It is at present used mainly in the manufacture of gas mantles. Its importance has now increased as it contains small quantities of thorium nucleus which may be used in the manufacture of atom bombs.

Kyanite: India is the principal producer of this mineral which is used mainly in the ceramic and refractory industries. It is to be found in the former Kharasawan and Sraikhela states and in Singhbhum, Bihar. Most of the domestic production is exported. Our annual production is about 27,000 tons.

Chromite: This is used mainly in the manufacture of refractory bricks and also in dyeing, calico printing etc. It is found in Mysore, Bihar and Orissa. About 46,000 tons were produced in 1961.

Bauxite: This mineral is used mainly in the manufacture of aluminium. We have large reserves of bauxite in Bihar, Madhya Pradesh, Western. ghats and deposits are also widely scattered all over the country. Reserves are estimated to be 250 million tons and the annual production was about 476,000 tons in 1961. Our total production of aluminium amounted to 3,566 tons, a small quantity as compared to our needs and resources. The main difficulty standing in the way of the utilisation of this mineral is the lack of cheap electricity.

Gold: 95 per cent of our gold production comes from the kolar gold mines in Mysore. Small quantities are also produced in Hyderabad. We produced about 4868 kilograms of gold in 1961.

Limestone: It is used mainly in the production of cement, in building construction and in the smelting of iron and lead ores.

Deposits of limestone are orderly scattered throughout India, especially in Bihar, Madhya Pradesh, Rajasthan, etc.

Petroleum: We produce only very small quantities of petroleum from the oilfields of Digboi in Assam.

Salt: It is produced by the evaporation of sea water in Madras, Bombay, Orissa and Kerala and from inland sources in Rajasthan. Rock salt mines are found in Mandi in Punjab.

We also produce China clay, fireclays, graphite, gypsum, lead, silver, sulphur etc.

In 1961 the total pitsmouth value of minerals produced in India was estimated at Rs. 1,65,69 lakhs, of which, the value of coal was Rs. 1,17,12 lakhs, that of gold and salt was about Rs. 6 crores each, of iron ore was about Rs. 10·21 lakhs and of copper ore was about Rs. 2·30 crores. We exported miscellaneous crude minerals of the value of 12·60 crores, to other countries. The average daily employment in mines was 652,000 and the value of the mineral output was nearly one per cent of the total national product.

The total value of mineral output in India in 1961 was Rs. 165·69 crores and the total foreign exchange earnings from mineral exports in that year were about Rs. 36·0 crores.

Review of the mineral position: Contrary to the popular belief, India is not rich in minerals. Our position is quite satisfactory in iron ores, mica, manganese, ilmenite and monazite. The position with regard to aluminium ore, limestone, refractories etc., may also be regarded as quite satisfactory. But we are deficient in such important minerals like copper, tin, lead and zinc, sulphur and petroleum. With regard to coal, the position is not bad, though the inadequacy of the known reserves of good quality coal is a factor of some anxiety. The concentration of coal in one part of the country is also a source of difficulty.

A second unsatisfactory feature is that the exploitation of minerals has so far been done mainly for purposes of export. The working of minerals has not been planned on sound and economic principles of development. There is a wide consensus of opinion that minerals should be treated in the country of origin as far as possible. It is, therefore, desirable to adopt a policy of co-ordinated, orderly and economic development of the minerals within the country.

Power resources: One of the most essential factors in the economic development of a country is the supply of cheap power. At present, the usual sources of power are coal, oil and electricity.

At one time or another, wind and woodfuel were also used as sources of power. But their importance is negligible.

Coal: Our position with regard to coal has already been examined. Our reserves of low-grade coal are quite ample for all purposes, while those of metallurgical coal may prove inadequate for the future. The main difficulty has been due to the excessive concentration of coal in the eastern parts of the country. As a result, industries in other parts have to pay higher prices for coal on account of the heavy cost of transporting coal by rail. It also results in much congestion of railway traffic, leading to the shortage of wagons in particular periods of the year. One way out of the difficulty is to establish thermal electric generating stations for utilising the low-grade coal whose stock is inexhaustible. This would ease the burden on the railways and result in the production of cheap electricity.

Oil: We are highly deficient in oil as we possess only one known oil-field at Digboy in Assam where small quantities of oil are produced. This deficiency may be remedied in two ways. First, like Germany, we may set up plants for the manufacture of synthetic petrol from low-grade coal. But this requires highly expensive plants as well as skilled labour. These are two important difficulties. A second way is to set up plants for the manufacture of power alcohol from molasses or starch like maize, potatoes, barley etc. Some attempts have been made in this direction and we are now utilising about 25 p.c. of the molassses for the manufacture of power alcohol. Recently the finding of oil in a number of other places (*e.g.* Cambay in Guzarat) has been reported.

Electricity: The importance of electricity as a source of power can hardly be overestimated. The provision of many of the amenities of modern life is bound up with the development and use of electricity. Many of the comforts of the modern home life such as electric lights, telephone etc., would have been unthinkable without electricity. Secondly, electricity, especially hydro-electricity, is one of the cheapest sources of power, and so is an essential factor in industrial development. There are certain industries which are specially dependent upon the provision of cheap electricity. The manufacture of aluminium from bauxite is economically possible only because of cheap electricity. Cheap power is also essential for the development of the heavy chemical industry. For this reason, some of the earliest projects under the Russian Five-Year Plan was concerned mainly with the generation of hydro-electric power.

There are reasons why the rapid development of electricity is essential in the case of India. First, the concentration of coal in the

eastern parts of the country has created many difficulties for industrial development. It has resulted in throwing a great burden on the railways of the country which had to transport coal to all parts with the consequent high cost of power. The development of cheap electricity in other parts of the country is therefore essential for securing a wider dispersal of industries than is possible at present. Secondly, the development of electricity is also necessary from the standpoint of agriculture. It will then be possible to produce cheap artificial fertilisers for the use of the cultivators. The various multi-purpose projects, combining irrigation with the generation of electricity, will provide cheap power. Lastly, the generation of cheap electricity will also foster the development of small-scale and cottage industries of our country. In Japan and Switzerland, many small-scale industries use electricity profitably with the production of cheap hydro-electric power. Our cottage and small-scale industries will also be able to utilise it and thereby lower their costs of production.

Present hydro-electric resources: India possesses large possibilities of hydro-electric development. But as yet only a small percentage of these resources has been utilised. The first hydro-electric plant was installed in 1897-98 at Darjeeling in West Bengal, followed by the completion of the Cauvery River Project in Mysore State in 1902. Since then some development has taken place in all states. The greatest hydro-electric works are the three schemes developed by the Tatas in Bombay, situated at Lonavala, Andhra Valley and Nila Mula. These projects have a combined normal capacity of 246,000 H. P., and provide electrical energy at low cost to the railways, mills and industries in the Bombay city. In Mysore, the Cauvery River Project is located at Sivasamudram with a capacity of 69,000 E. H. P., which is supplied to the Kolar gold fields, Mysore, Bangalore, and about 200 other towns and villages in the state. In Madras, there are three hydro-electric schemes, *viz.,* the Pykara hydro-electric schemes, with an estimated capacity of 40,000 K. W., the Mettur Dam Project with a capacity of 50,000 K. W., containing the largest Dam in the world, and the Papanasam hydro-electric schemes with a capacity of 21,000 K. W. In Punjab, the Mandi hydro-electric works have an installed capacity of 118,000 K. W. In U. P., the Ganges Canal hydro-electric gird supplied power at cheap rates to some 93 towns in 14 districts, besides providing energy for irrigation pumping. In the state of Jammu and Kashmir, there are three hydro-electric schemes, the first of which was started in 1909 on the river Jhelum. As a result, *per capita* generation of electricity in India increased by about 10 p.c. between 1938 and 1953.

In spite of this development, only a small percentage of the potential water-power resources of India has been utilised. Our potential water-power resources have been estimated to amount to about 30 to 40 m. Kwt, which are exceeded only by the USSR. Of this amount barely 1·5 per cent has been developed. No wonder that the *per capita* consumption of electricity is probably the lowest in India, being 31·6 Kwt as compared to 3836 Kwts in Canada, 3752 Kwts in Norway, 2880 Kwts in the U.S.A., 2400 Kwts in Sweden, 832 Kwts in the U.K., and 527 Kwts in Japan. Unfortunately, most of the development of electricity in India has taken place to satisfy the needs of the urban areas. Bombay and Calcutta consume between them about 40 p.c. of the total power produced, and only towns with a population of 20,000 or upwards are now supplied with electricity. Consumption of electricity is practically insignificant in the rural areas, as only two villages out of seven have been supplied with electricity, and that too is confined mostly to Mysore, Madras, and U.P. Upto 1960-61 about 22,985 villages and towns have been electrified.

New hydro-electric development: In recent years increasing attention is being paid by the Government of India to the task of developing hydro-electric resources. The five-year plans lay down great emphasis on this aspect of development, and the projects included in the plans are expected to generate an additional amount of 1·46 m. Kwt, of electrical energy, besides providing irrigation for large areas. A brief description of some of these projects is given below.

In Punjab, the most important hydro-electric project is the Bhakra-Nangal Project, which is estimated to cost about Rs. 175·6 crores. The total generating capacity of this project will be about 604,000 Kw. and this will provide electricity to about 67 towns in Punjab, besides irrigating 67 lakh acres of land.

In West Bengal, the most important scheme is the Damodar Valley Project, which, by harnessing the water of the river Damodar, is expected to generate about 300,000 Kw. In Orissa, the Hirakund Dam Project is estimated to generate 1,23,000 Kw. by building a dam across the river Mahanadi. In Bihar, the Koshi Project will generate 1·8 m. Kw. The Tungabhadra Project is a joint undertaking of the Governments of Andhra Pradesh and Mysore. In U.P., the most important scheme is the Pipri Dam and Power Station Project, which, by building a dam across the river Rihand, is expected to generate 230,000 Kw. Another important scheme is the Jamuna Hydro-electric Project, which is expected to produce between 40,000 to 50,000 Kw. of electrical energy. In Bombay, the most important scheme is the Kayna Hydro-

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electric Project where one of the largest generating units is going to be constructed, generating 250,000 Kw.

Besides these important projects, quite a large number of minor schemes are being carried out in different parts of the country. In order to regulate the development of electricity, the Government of India have passed the Electricity Supply Act in 1948. Under this Act, the state has assumed control over the generation and distribution of electricity in India. In order to co-ordinate the development, provisions have been made for the setting up of a Central Electricity Authority and of State Electricity Boards. The Central Electricity Authority, which has already been set up, has been entrusted with the duty of co-ordinating and promoting all schemes of development of electricity in consultation with the State Electricity Boards. The State Boards have also considerable autonomy subject to the over-all co-ordination by the Central Electricity Authority.

By 1960-61, the installed capacity for power generation was 4·68 million kw. as against 2·69 million kw. at the beginning of the Second Plan. About 17,400 small towns and villages will be electrified. According to the Third Plan proposals, another 15,000 villages and small towns will be electrified, bringing the total to 32,000 in 1965-66. Thus by the end of the Third Plan, the number of rural centres electrified is expected to be doubled.

Agricultural resources: As India possesses large variety of soils and climatic conditions she grows almost all the important crops. We shall now study the general position regarding agricultural crops.

According to the details given in the Five Year Plan, the total geographical area of India consists of 811m. acres, of which statistics are available for only 615m. acres. Of these, the cultivable area comprises about 324m. acres, consisting of 266m. acres of net area sown and 58m. acres of current fallows. Of the total cropped area about 78 p.c. grows food crops, 17 p.c. grows commercial crops and 1·1% grows plantation crops and spices.

TABLE I

CROP PATTERN	ACRES	PERCENTAGE OF THE TOTAL CROPPED AREA
Food Crops		
Cereals	193·04m.	60·58
Pulses	28·47m.	8·98
Gram	18·71m.	5·9
Fruits and Vegetables ..	5·00m.	1·58
Other Food Crops ..	1·65m.	0·52
	246·87m.	77·86%

CROP PATTERN	ACRES	PERCENTAGE OF THE TOTAL CROPPED AREA
Commercial Crops		
Major Oil seeds	26·68m.	8·41
Other Oil seeds	4·27m.	1·36
Cotton	14·56m.	4·50
Sugarcane	4·21m.	1·33
Jute	1·41m.	0·46
Other fibres	1·05m.	0·33
Tobacco	0·90m.	0·28
	53·12m.	16·75%

CROP PATTERN	ACRES	PERCENTAGE OF THE TOTAL CROPPED AREA
Plantation Crops	1·19m.	0·37
Condiments and spices	2·46m.	0·78
	3·65m.	1·15%
Other Crops	13·44m.	4·25%
Total Cropped area	317·08m.	100%

We shall now discuss each of the principal crops in detail.

Food crops: (1) *Rice.* India is the second largest producer of rice, the first being China. The area under rice in India is about one-third of the total world acreage under rice, whereas her output is only one-fourth of the world production of rice. The average yield per hectare is 1220 kgs. of paddy in India as against the world average of 1650 kgs. In 1965-66 about 31·8m. hectares were under rice as compared to about 16·9m. acres under jowar and 10·4m. hectares under Bajra. It is the staple food of the people in the southern and eastern parts of the country. But in spite of such a large output (38·17m. tons in 1965-66), India has to import rice from other countries in order to feed her population. Imports come mainly from Burma, Thailand, etc.

(2) *Wheat.* The second important food crop is wheat, which was cultivated on about 12·18m. hectares of land in 1965-66. The total yield has been estimated to be 12·1m. tons in 1965-66. Among the wheat producing countries of the world, India occupies the third place in respect of acreage (the first two being the U. S. A., and Canada), and sixth in respect of the total yield. This shows that the average

yield per acre is much lower in India than in many of the important wheat-producing countries. As a result, India has to import large quantities of wheat from other countries.

(3) *Millets.* Of the millets, Jowar and Bajra are most important. These are grown more commonly in the dry areas of Madras, Bombay, M. P. and U. P. etc. These are consumed mostly by the poorer classes in these areas. In 1965-66 about 16·9m. hectares were under jowar, and 10·4m. hectares were under Bajra. Unfortunately we have also been forced to import these inferior food crops.

(4) *Barley.* It was grown on about 2·5m. hectares in 1965-66 of which about 2m. acres were in U.P. The next important state growing Barley is Bihar where about 1·10m. acres were under this crop. Though counted among food crops, this is used mostly in making malt and beer. In early days, India used to export some barley. But we have now to import it in many years.

(5) *Pulses.* Various pulses like gram, masur, arhar etc. are grown all over the country. Gram is the most important of these crops, and was grown on about 7·9m. hectares of land in 1965-66 as compared to 17·9m. hectares under other pulses. Gram is grown mostly in Punjab, U. P., Bihar, M. P. etc.

Commercial crops: These consist of the fibres like Cotton and Jute, Oilseeds, Sugarcane etc.

(1) *Cotton.* Quite a large area (7538 thousand hectares in 1965-66) was under this crop, and the total output was estimated to amount to 54 lakh bales. It is grown mostly in the Madhya Pradesh, Guzarat, Madras, etc. Before the partition of the country in 1947, India used to export considerable quantities of raw cotton, mostly short-stapled. But after the partition, the major portion of cotton-growing areas were in Pakistan, and so India has to import raw cotton, both of the short-staple and long-staple variety, from other countries. Of the cotton grown in India, the major portion is of the short-staple variety, though attempts are being made to grow the long-staple variety as well.

(2) *Jute.* Undivided India had a monopoly in the production of raw jute. But the partition left India with only less than one-third of the previous acreage under jute. Following the Indo-Pakistani dispute, India has made great efforts to grow more jute, and as a result, the area under jute has increased from 834,000 acres in 1947 to 1707,000 acres in 1964-66. It is grown mostly in West Bengal, Bihar, Assam and Orissa. While India has still to import large

quantities of raw jute from Pakistan, she is the largest exporter of manufactured jute goods. The area under jute and mesta in 1965-66 has been estimated to be 10·7,000 hectares. The production was 750m. tons.

Oil-seeds. The most important oil-seeds are groundnut, castor, rape seed, linseed, mustard, etc. Groundnut was grown on about 7171 thousand hectares in 1965-66, and the total output was estimated to amount 5·9m. tons. It is grown mostly in Madras, Maharashtra, Madhya Pradesh etc. India exports large quantities of groundnut mostly to the European countries, though in recent years, the amount of exports of groundnut oil is increasing. Sesamum was grown on 1565 thousand hectares and linseed on 1144 thousand hectares; rape and mustard seeds were grown on 1191 thousand hectares. Both linseed and its oil are exported mostly to Australia, Italy and other countries. U. P. is the leading producer of Sesamum, which is exported mostly to the European countries. Rape seeds, grown mostly in Northern India, *e.g.* Bihar, U. P., Punjab etc., is exported to the U. K., France and other European countries.

(3) *Sugarcane.* India is the largest producer of sugarcane in the world. The total area under this crop was about 2·59m. hectares in 1965-66 and the output was estimated to be 12315 thousand m tons of sugar. The chief cane-growing areas are the U.P., Bihar, Maharashtra and Madras, whose shares in production are 53·2 p.c., 20·7 p.c., 10·5 p.c., and 6·1 p.c. respectively. There are about 157 sugar factories in India.

(4) *Tobacco.* It was grown on about 423 thousand hectares in 1965-66 and the output was estimated to be 358 thousand tons. India is the third largest producer of tobacco in the world. It is cultivated all over India, though the chief tobacco-growing areas are to be found in Madras, Maharashtra and Bihar. Madras produces the best virginia tobacco. There are large exports of tobacco. It is exported to about 32 countries and fetches on average about Rs. 18 crores of foreign exchange.

Plantation crops: (1) *Tea.* India stands second in the world both in respect of acreage and yield of tea. It is grown mostly in Assam, North Bengal, South India and certain areas of Punjab.

(2) *Coffee.* Coffee is grown mostly in Mysore state, and Madras.

(3) *Rubber.* It is grown mostly in Madras, Mysore and Kerala. The total area under rubber was 155,000 hectares and the annual output was estimated to be 27000 tons. India is deficient in rubber and has to import large quantities from Malay and other countries.

(4) *Cinchona.* It is grown on government plantations in Darjeeling and the Nilgiri hills. Production is short of the needs of the country and India has to import considerable quantities of cinchona.

Over-all agricultural situation: Of the more important crops, jute, oilseeds and tea are important export crops. Though we produce large quantities of food crops, we are deficient in that respect, and have to depend on imports. The production of important industrial raw materials like raw jute, raw cotton etc., is also not sufficient to meet the needs of our industries, and here also we have to import them in large quantities. The position is not at all happy. Nor is the trend in regard to production a bright one. As the Planning Commission pointed out, the area under foodgrains has shown only a small increase in the forties. Although the gross cropped area had increased as a result of double cropping, little new area has come under cultivation during the last decades. The trend regarding the yield of crops is also indefinite. In regard to commercial crops, the yield is tending to increase. But in respect of food crops, "yields show an increase for certain crops in certain states, a decline in certain others and absence of any perceptible change in the rest."

The position with regard to agricultural production was much better in 1960-61 as compared to the earlier year, and the index number of agricultural production rose to 139·0 (base 1949-50=100), and this was higher by 5·3% over the previous record of 132·0% in 1958-59. The total output of foodgrains amounted to 79·3m. tons of which the output of cereals was 66·8m. tons. The output of rice has increased from 24·9m. tons in 1957-58 to 33·7m. tons in 1960-61. But in spite of this overall improved position, the prices of agricultural crops increased from an average of 107·4 in 1957-58 to 120·0 in 1960-61, *i.e.,* a rise by more than 11·7 p.c. on account of the larger increase in the demand for these goods.

Forest resources: Forests also constitute an important source of wealth. Sweden, Finland, Norway and Canada earn large sums of money by selling timber to other countries. Unfortunately India's forest resources are not large in comparison with her size. The present area under forests has been estimated at 2·80 lakh sq. miles, which is 22 p.c. of the total land area. This is low compared to other countries. The percentage of forest lands to total lands also varies in different states from 74·3 p.c. to 12·3 p.c.

There are five different types of forests in India,—viz., *evergreen forests* of teak, ebony, bamboos etc.; *deciduous forests* of the Deccan containing teak, sal, sandal wood etc., *dry forests* of Rajasthan and

Punjab, consisting mostly of shrubs, *hill forests* of oak, deodar, pines, fir etc. ; and *littoral forests* found in the deltas of the rivers, the Ganges, the Mahanadi etc. The Government has classified forests into four groups ; *viz.*, protective forests which are necessary for the prevention of soil erosion and floods ; timber forests which yield large revenue ; minor forests which supply mainly fuel, fodder etc. ; and pasture land. They are further classified into reserve forests, protected forests and unclassified forests. *Reserve forests* are controlled strictly by the government. In *protected forests* the local population have rights of grazing and fuel and fodder cutting under the supervision of forest officers. In *unclassified forests* there are no restrictions.

Forest products are of two types, major and minor. Major products are timber and fuel wood. The principal varieties of timber are sal, teak or sagun, deodar, toon, jarool etc. Minor products are the essential oils, dyeing and tanning substances, gums and resins, lac, beewax and honey etc. Oil trees are sandal wood found in South India. The gum and resin yielding trees are babul, catchu, sal, pine, mango and banyan. The most important tanning material is myrabalan. Beewax is used mainly in candles, calico-printing, medicines etc. Another important forest product is lac, which is produced mainly from certain classes of tree grown in M.P., Bihar, Assam etc. It is used extensively in the manufacture of gramophone records, plastics, sealing wax etc., and is exported in large quantities.

Utility of forest : Forests play a very important role in the economic organisation of a country like India. They are an important source of wealth. They supply timber for building purposes and fuel and fire wood for industrial and domestic purposes. They provide raw materials for the match-wood, ply-wood and paper industries. A large number of forest products like lac, tanning materials etc., are exported to foreign countries, and, therefore, bring in valuable foreign exchange. Lastly, they also provide grazing grounds and fodder for cattle. In addition to these direct advantages, forests are highly important to an agricultural country. Forests influence the climate and induce rainfall. They prevent soil erosion and so add to the fertility of land. Forest leaves fall on the ground and manure the land. They regulate air currents. They absorb moisture and provide protection against the occurrence of floods. It has been stated that the deforestation of the hills in India is one of the most important causes of floods in our country.

Forest Policy in India : The important role played by forests has come to be recognised only in recent times. A consistent forest policy

was adopted by the Government of India only from 1894. Previous to that period there was reckless destruction of forests, thereby increasing the incidence of drought, flood and soil erosion. But the old forest policy was defective on the ground that it looked upon forests mainly as an important source of revenue, though it recognised that the retention of sufficient forest areas was of primary importance for the purpose of preservation of the climatic and physical conditions. The Planning Commission rightly recognises the need for a positive policy for the administration and utilisation of forests. Attemps should be made to increase the area under forests and afforestation measures should be adopted on a large scale to prevent soil erosion. Along with this, attempts are to be made to utilise the forest products to the fullest extent possible and to develop the forest industries.

The Government of India have set up a Central Board of Forestry in 1950 for the purpose of evolving a common policy throughout India. The main functions of the Board are to co-ordinate the forest policies adopted by the different States to regulate and develop forests in inter-State river valleys which are now the concern of the Central Government, to co-ordinate forest research etc. In the same year, the government initiated the *Vana Mahotsava* ceremony, during which trees are to be planted throughout the country.

Fisheries: India has also a large number of fisheries distributed over about 3,000 miles of its coastlines and many rivers and ponds. It has been estimated that these fisheries contribute about Rs. 27 crores to the national income per year, give employment to some 750,000 fishermen and engage about 75,000 crafts of various types. Recently attempts are being made to develop sea-fishing on modern lines.

Conclusion: This study shows that though our total resources are comparatively large, these have not been developed to the desirable extent. The Indian economy is as yet undeveloped, as a result of which the per capita annual income is very low as compared to that of some of the industrially advanced countries. There has, of course, taken place some amount of industrial development in the last four or five decades. But judged in terms of the country's needs and potentialities, the development is only partial and limited. There has been virtually no advance in agricultural production. Old cottage and small-scale industries have been decaying and there is chronic underemployment in the rural areas. At the same time, population has grown rapidly. The result has been the continuation of the poverty of the people. What is now needed is the adoption of measures for the simultaneous

development of all parts of the economic system according to a pre-determined plan.

Questions

1. Describe the principal mineral products of India with special reference to their location. Point out the utility of each for industrial development. (Ag. 1935 ; All. 1932 ; Punj. 1957 ; Cal. 1947, 1939).

2. Describe the various sources of power in India, and point out the importance of their utilisation for the development of industries. (Ag. 1940 ; All. 1940 ; Pat. 1957 ; Punj. 1940 ; Cal. 1933).

3. Mention the principal agricultural crops of India. State their regional distribution and indicate their importance in the foreign trade of India. (Cal. 1936 ; Punj. 1934 ; Nag. 1939).

4. Estimate the importance of cash crops to our rural economy. Should we grow more food at the expense of cash crops ? (Cal. 1945).

5. Describe the forest resources of India and point out their economic importance. (Ag. 1957 ; Punj. 1958 Supp. ; Cal. 1950 ; Mad. 1938).

6. Comment on the statement that India is a rich country inhabited by poor people. (Del. 1956 ; Punj. 1954).

CHAPTER 4

POPULATION AND ITS GROWTH

The population of India is 439·24 millions according to the census of 1961. This figure includes the population of Manipur, Sikkim and of the Tribal areas of Assam. It also includes the population of Jammu and Kashmir, Goa, Daman and Diu, Dadra and Nagar Haveli, and Pondicherry. India occupies the second highest place in respect of population, the first being China with a population of 60 millions. It is interesting to study the rate of growth of population in the twentieth century.

Table 1

YEAR		POPULATION (*in millions*)	INCREASE (*in millions*)	PERCENTAGE *Increase*
1901	..	235	..	..
1911	..	250·7	15·7	+ 5·7
1921	..	250·0	−0·7	− 0·3
1931	..	277·4	27·4	+11·0
1941	..	316·9	39·5	+14·2
1951	..	359·2	42·3	+13·3
1961	..	436·4	77·2	+21·5

It will be seen that during the last 20 years, 1931-51, the increase in population has been about twice the number added during the 30 years 1901-1931. According to the published figures of the census of 1961 the rate of growth is 61 p.c. faster than that in the preceding decade.

Growth rates in other countries: The following table shows the rates of growth of population in a number of countries in the World.

Table 2

COUNTRY	ANNUAL GROWTH RATE (1950-60) %
Australia	2·3
Canada	2·9
France	0·9
West Germany	1·1
Ceylon	2·5
Japan	1·2
U. K.	0·4
U.S.A.	1·7

The growth rates are no doubt higher in Australia and Canada than that in India. But these are rich countries with small populations. Canada's population is, for example, increasing annually by only 0·48 millions whereas India's population is increasing annually by 9·37 millions.

Population in different States: As regards the total population, Uttar Pradesh has the highest number with a total of 73·8 millions, followed by Bihar, (46·5 millions), Maharashtra (39·5 millions), Andhra (36·0 millions), Madras (33·7 millions), West Bengal (35·0 millions) etc. U.P. has a larger population than the U.K.

The rate of growth has also been different in different States. The highest increase has taken place in Assam (34·3 p.c.), while the lowest is in Jammu and Kashmir (9·7 p.c.).

Table 3

State	Population (*millions*)	State	Population (*millions*)
U. P.	73·8	Rajasthan	26·1
Madras	33·7	Orissa	17·6
Bihar	46·5	Guzarat	20·6
Maharashtra	39·5	Punjab	20·3
West Bengal	35·0	Kerala	16·9
M. P.	32·4	Mysore	23·5
Andhra Pradesh	36·0	Assam	11·9

Density of population in India: Density of population is determined on the basis of the number of people who live on one square mile on the average. This is found out by dividing the total population by the total area of a country. The average density of population in India is 384. This figure is 40 p.c. higher than the density of population in Europe excluding the USSR. The average density of population is nearly 600 in the U.K., 654 in Belgium and 449 in Germany. But these are highly urbanised, whereas India is predominantly a rural country. The density of population in the villages of India is about twice as high as that of rural Europe. If we compare the Indian density with that of other agricultural countries, we shall find that the Indian figure is rather high.

Table 4

Country	Density of Population
India	384
China	123
Indonesia	108
Brazil	15

The Indian figure is also very high in relation to some agricultural-cum-industrial countries, such as Australia and Canada where the density is 3 per sq. mile, or France where it is 193 per sq. mile. In the U.S.A., density is only 50 per sq. mile.

Density of population in the States: The density of population varies enormously between different States. This will be evident from the following table :—

Table 5

State	Density of Population
West Bengal	1,032
Bihar	691
U. P.	641
Madras	669
Punjab	430
Maharashtra	333
Mysore	318
Orissa	292
Guzarat	286
Madhya Pradesh	189
Rajasthan	153
Assam	252
Andhra	339
Kerala	1,127

There are many factors that account for these variations in density. There is, first of all, the influence of the configuration of the land. Areas which are hilly and mountainous contain a sparse population, whereas the density of population is high in the level plains. The hilly regions in the north of India have smaller density of population than the plains of Bihar, U. P., and West Bengal. A second important factor is the facilities possessed by the region for agricultural development. As the vast majority of the people depend on agriculture for their livelihood, they naturally flock to those places where the rainfall is abundant, or where there are good irrigation facilities and where the soil is most fertile. Thus the plains of West Bengal, Bihar and U.P., where rainfall is more or less adequate and the soil is fertile, contain the highest density of population for an agricultural country. Density

of population has increased in those areas like Punjab after the construction of irrigation works. These factors also explain the low density of population in Rajasthan where rainfall is scanty and the soil conditions are unfavourable. Why is it that Assam where rainfall is plentiful, has the lowest density of population ? The explanation is to be found in the influence of the climate and the configuration of the land. Assam has a unhealthy climate and large areas of hilly land with jungles. Lastly, the density of population is also influenced by the extent of growth of industries in a region. Areas which contain a large number of factories also show a high density of population.

Occupational distribution of population: The occupational distribution of the population provides an index of the economic progress of a country. As countries become highly developed, a larger percentage of the population becomes occupied in tertiary industries like commerce, transport services etc. ; and a smaller percentage depends on primary industries like agriculture, forestry etc.

The occupational distribution of the population of India shows the relatively undeveloped nature of her economy. In fact, the recent tendency has been some increase in the percentage of population engaged in primary production. In 1931, 68·84 per cent of the total population was engaged in agriculture, whereas by 1961 the percentage has increased to 69·8.

Table 6

Occupational distribution in 1961

Percentage engaged in	1931	1961
Agriculture	65·84	69·8
Industry	10·38	10·5
Commerce	5·83	5·9
Transport	1·65	1·5

This should be compared with the percentage of population engaged in agriculture in other countries. It was 6 p.c. in the U. K., 19 p.c. in the U. S. A., 17 p.c. in Belgium, 24 p.c. in Sweden, 20 p.c. in New Zealand, 16 p.c. in Australia and 26 p.c. in Canada.

Table 7 contains figures of percentage of agricultural population to total population in the different States of India.

Table 7

STATE	PERCENTAGE
West Bengal	57·2
Bombay (United)	61·5
Punjab	64·5
Madras	64·9
Rajasthan	70·9
Assam	73·3
U. P.	74·2
M. P.	76·0
Orissa	79·3
Bihar	86·0

Distribution between Town and Country: Like the occupational distribution of population, the percentage of people living in the urban areas is an index of the industrial progress of a country. As a country becomes more and more industrialised, a larger percentage of the population will be found to be living in the urban areas. For example, in the U.K. about 80 p.c., of the population live in towns. In France which maintains a balance between agriculture and industry 52 p.c. of the people live in the urban areas.

As compared to these countries, the percentage of population of India living in towns is comparatively small. It is only about 18·0 p.c. in 1961. In the two most industrialised States of Maharashtra and West Bengal, the percentage of urban population to the total population is only 27·9 and 23·2 respectively. While this clearly bears out the low state of industrialisation achieved by the country, there are certain indications that the rate of urbanisation is definitely increasing in the last two or three decades. Coming to over-alll figures, the percentage of urban population has increased continuously from 11·4 p.c. in 1921 to 12·1 p.c. in 1931, 13·9 p.c. in 1941, 17·3 p.c. in 1951 and 17·8 p.c. in 1961. Cities containing one lakh or more population have increased in number from 58 in 1941 to 107 in 1961, and their aggregate population has also increased from 16·748 m. in 1941 to 24·085 m. in 1951, an increase, by about 50 p.c. as compared to the general increase of 13·4 p.c. during the same period. These tendencies point to an unmistakable shift of the population from the rural to the urban areas.

Age groups: The distribution of population between different ages can be represented as a pyramid with a broad base and a gradually

narrow top. The number of children born represent the base,—the lowest age group. The height of the pyramid represents advancing age groups. As the people lie at different ages, the top of the pyramid becomes narrower. In India, the base of pyramid is very broad, whereas it tappers off sharply at the top. This is due to the fact that the birth-rate is very high in our country, and so a very large number of children is born, broadening the base of the pyramid. But as the death-rate is also very high, the shape of the pyramid is extremely narrow. There is a large concentration of population of the lower age-groups and a small survival at the higher age-groups. Thus the number of people below 15 years of age constitutes 38·3 p.c. of the total population of India against 27·1 p.c. in the U.S.A. But people who are above 55 years constitute only 8·3 p.c. of the population in India against 16·9 p.c. in the U.S.A., and above 21 p.c. in France and the U.K.

The immediate aim of the study of age groups is that it would give an idea of the population for which educational facilities upto the age of 15 have to be provided. It would also indicate the approximate number of people who attain working age year to year as against the numbers who complete their working age. We may then estimate the net additions to the working population for whom new jobs have to be found.

Sex ratio: The sex ratio, revealed in the census of 1961 as also in previous censuses, shows a general excess of males over females, (940 females per 1000 males) and this has long been regarded as peculiar to India. The explanation is that in India, more male children are born than females. Upto the age of 12, mortality rate among females is less than that among males. But in foreign countries more males die than females after this age, as a result of which there is an excess of females over males in later ages. But in India mortality rate among women of reproductive age is so high that there is in later ages more males than females. Only in the two States of Orissa, and Kerala do females outnumber males. On the other hand, the proportion of females per 1000 males is as low as 868 in Punjab, and 877 in Assam. This is the result of very high female mortality rate.

Birth rates: There are a few points to be noted in relation to the birth rate in India. In the first place, until the year 1941, the birth rate remained more or less steady, though it fell in every other industrially advanced country. Secondly, since 1941 there has taken

place some decline in the birth rate, though after this decline it has remained more or less steady. Lastly, even after this decline, the Indian birth rate is one of the highest in the world. These points will be evident from the following tables.

Table 8

Birth rate per 1000 population in India.

1881-91	1921-25	1931-35	1938-41	1945-49	1956-61
45·9	44·7	44·3	42·5	42·1	40·7

Between 1881 to 1935, the average birth rate declined from 32·5 to 15·5 in the U.K., and from 36·8 to 15·9 in Germany. The Indian birth rate remained above 40 till 1941 and then has only declined only slight since then. It has remained steady round about 40 in the 6 years, 1956-1961

Table 9

COUNTRY	YEAR	BIRTH RATE PER 1000 POPULATION
India	1956-61	40·0
W. Germany	1960	17·7
Italy	1960	18·5
Canada	1960	26·8
U. K.	1960	17·5
Japan	1960	17·1

There are, of course, other countries where the birth rate is higher than that in India ; for example, in Ceylon (40·6), Egypt (42·6), Mexico (44·6), Phillippines (32·4) etc. According to some writers, *e.g.*, Dr. Gyanchand, Mr. D. Ghosh, the Indian birth rate is underestimated as not all births are reported to the authorities. The actual birth rate would be in the neighbourhood of 40 and above.

What are the *causes of such high birth rates* ? It is remarkable that the birth rate is so high in India in spite of the fact that there are certain factors which actually retard births. For example, the practice of early marriage often results in some women becoming widows at an early age. The absence of widow re-marriage is also an important factor which ought to lead to smaller birth rate. Moreover,

the practice of prolonged lactation and the wide-spread prevalence of many diseases lower the vitality of people and so impair the fertility of women. But in spite of these factors, the birth rate is undoubtedly high. The main cause of such a high birth rate is the prevalence of the practice of universal and early marriage in our country. In the opinion of many experts, fertility is comparatively high for women between the ages 15 to 30. About 80 p.c. of the girls between the ages 15 to 30 are married in India against 41 p.c. in the U. K. Thus a larger percentage of girls is married in the most fertile period of a woman's life in India than in the western countries. Lastly, the wide-spread adoption of birth control practices is responsible for lower birth rates in the western countries. But the vast majority of the Indians are both too ignorant and too poor to adopt birth control in any form.

Death rates: While the fall in the birth rates in India has been comparatively slow in India, the death rates have, however, declined by a larger percentage. This is evident from the following table.

Table 10

	1881-91	1921-25	1931-35	1945-50	1956-61
India	27.4	26.0	23.8	22.5	21.6

Thus the death rate has fallen by a substantial percentage between the years 1931 to 1951. This is due to the improvements in medical services in the country. But in spite of this decline in the death rate, it is substantially higher than that in the advanced countries.

Table 11

COUNTRY	YEAR	DEATH RATE
India	1956-61	21·6
U. K.	1960	11·5
Australia	1960	8·6
Canada	1960	7·8
U.S.A.	1960	9·4

This high death rate is due to the comparatively high rates of infant and female mortality. While *the rate of infant mortality* per 1000 live births is 142 in India in 1956-61, it is only 21·5 in Australia (1960), 26·4 in the U.S.A. (1960), and 23·1 in the U. K.

(1960). The Indian rate is exceeded only by Burma where it was 203·8 in 1939, Egypt (138·6 in 1948) and Columbia (134·1 in 1949). In India about one-fifth of the children die before they reach the age of one, and about one-fifth of the total deaths is due to the infant mortality. This high rate is due primarily to the low vitality of the mothers on account of poverty and lack of sufficient food, congestion in cities and ignorance and lack of care of children.

The *death rate among women* of reproductive age is also very high in our country. According to the Public Health Commissioner for India, the possible death rate among women is 20 per 1000 child births, whereas the figure is about 3 for the U. K. This is certainly alarming and shows a huge waste of life in our country. This high female mortality rate is due to a variety of reasons, such as the lack of proper medical care during and after child birth, poverty and malnutrition coupled with excessive pregnancy. A woman's life is held cheap in India even by the women themselves and not much attention is paid to give proper diet and medical care to the women members of the family even among the well-to-do classes.

Expectation of life: The result of such high death rates is the extremely low expectation of life in India as compared to that in other countries.

Table 12

COUNTRY	AVERAGE EXPECTATION OF LIFE
India	42·00
Egypt	35·65
Mexico	37·92
Australia	66·02
Canada	65·18
Sweden	67·06
U. K.	66·39

Thus the average expectation of life in India is probably one of the lowest in the world. This is due to the high rates of infant and female mortality and to the extremely low standard of living of the general masses. Moreover, while in other countries the average expectation of life is higher among females than that among males, the situation is just the opposite in India.

Table 13

COUNTRY	AVERAGE EXPECTATION AMONG MALES	AVERAGE EXPECTATION AMONG FEMALES
India	42·00	40·00
Egypt	35·65	41·48
Australia	66·07	70·63
Sweden	67·06	69·71

One encouraging feature is that the latest figures of the average expectation of life in India on the basis of post-1961 data record a further increase in expectation of life to 50 years. According to the 1931 census, average expectation was 26·91 among males and 26·56 among females. The lower average expectation of life among women is probably due to (a) the social custom of bestowing better care on male children, and (b) the impact of high maternal mortality between the ages 20 to 45.

Net reproduction rate: While a study of the average birth and death rates is important, it does not enable us to know the correct trend of the growth of population. The best method for this purpose is the determination of the net reproduction rate, a concept stated by Mr. Kuczynski. This concept is based on the following idea. If we want to know whether each generation is reproducing itself or not, we should find out the total number of only female children born to, (say), 1000 women throughout their reproductive period. If 1000 women give birth to 1000 female children who grow up and complete their reproductive age, it means that each generation is exactly reproducing itself. The net reproduction rate is then equal to unity. If more than 1000 female children are born and grow up, the net reproduction rate is more than one. This will indicate that the present population is more than reproducing itself.

The net reproduction rate is found out, first, by calculating the number of female children born to 1000 women on the basis of the present fertility rate, assuming that each women lives throughout her reproductive period. This figure is then to be corrected on the basis of mortality tables. We have to make allowance for the fact that as women grow up, a certain number of them die at each stage before completing the full reproductive period.

Unfortunately we do not possess enough statistics to find out the net reproductive rate for India. A number of writers have, however,

tried to determine this rate on the basis of certain hypotheses. Mr. D. Ghosh has calculated the net reproduction rate to be 1·1 in India. In other words, the Indian population is increasing by 10 p.c. in each generation. The National Planning Committee estimated a higher figure. According to the Committee the rate is 1·45 for India. These estimates are, however, merely tentative.

Future Growth: In a recent book, Coale and Hoover* have made an estimate of the future population of India on the basis of certain assumptions regarding the birth and the death rates. According to the first assumption the present fertility rates are likely to continue in the future, and this would mean that India's population would grow to 775 millions in 1986, growing at the rate of 2·6 p.c. per year. A second estimate was made on the basis of the assumption that fertility rates would decline by 50 p.c. between 1956 and 1981, and the total population would then number 590 millions growing at the rate of 1 p.c. per year. A third estimate had been made on the assumption that fertility rates would start declining only after 1966 and would decline by 50 p.c. between that year and 1981. In that case the total population would amount to 634 millions. Of the three assumptions, the second is extremely unlikely as a rise in the standard of living is more likely to raise the birth rates than to lead to a decline. On the other hand, death rates would decline considerably in view of the improvements in medical science and the impact of a better standard of living. So the actual growth of population would probably lie between the first and the third estimates.

The question of over-population: The question, whether India is over-populated or not, is a most controversial one. In order to have a clear idea on this subject we propose, first of all, to review certain broad facts about the growth of population in India. The population of India has grown by about 74 p.c. in the first 60 years of this century. The rate of growth was comparatively slow until 1921. But in the last 40 years, the pace of growth has been accelerated. Both the average birth and death rates are very high. Though of late, birth rates have declined to some extent, the fall in the death rates has been larger, thereby resulting in considerable growth of population. But while population has thus been growing, neither the volume of food production nor the standard of living of the masses gives any indication of substantial improvement. High birth rates, high death rates, inadequate food-supply and backward living conditions—these are all symptoms of the existence of the population problem in India.

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* A. J. Coale & E. M. Hoover. *Population Growth and Economic Development in Low-Income Countries.* 1958.

Quite a large number of writers have, on the other hand, expressed the opinion that our country is not over-populated. They point to the fact that though the population of India has grown by 52 p.c. between 1901-1951, this is lower than the rate of growth in the European countries. Thus during 1880-1930 the population of India increased by only 39 p.c., while that of the U. K. rose by 54 p.c., of Japan by 74 p.c., and that of the U.S.A. by 186 p.c. Secondly, the density of population is also smaller than that in many other countries like the U. K., Belgium etc. Thirdly, estimates of per capita income framed at different periods in our country, show that it is rising, though of course at a very slow rate. Lastly, India, it is claimed, has large natural resources, which are to be found in very few countries.

While these arguments influence a large number of individuals, it should be remembered that it was not always the growth in percentages but the actual growth in numbers of people who had to be fed that was significant. The growth of population, calculated in terms of percentages, may be less in India than in the European countries. But as India's population is already very large, growth in small percentages means actually increase in large numbers. The relevant question is, whether the growing population can be supported by the available resources of the country without a lowering of the general standard of living. The population of Europe has no doubt increased by a larger percentage. But so great has been the pace of economic development in Europe that the standard of living of the masses actually rose during the period. So the rate of growth of population has to be compared with the rate of economic development. Judged by this test, the case against over-population is not very hopeful. There is no evidence that the average standard of living has risen in India during the last 50 years, in spite of a small problematical increase in the per capita income. The foodsupply has not grown in proportion to the growth in population. The area under foodgrains decreased from ·87 acres per head during 1913-14 to ·61 acres per head during 1942-43. While the population of India increased by 27 p.c. during the 20 years 1921-41 there has been a decline in the cultivated area by 5·8 p.c. during the same period. The extent to which the growth of industries, trade and commerce has afforded avenues of employment to the growing population is, however, comparatively small. In spite of the expansion of a few industries like iron and steel, cotton, sugar, jute etc., industrial employment has not increased materially in the country. As a result, the pressure of population has increased in the rural sector and this is borne out by the statistics of occupational distribution furnished by the 1951 census, according to which, the percentage of population dependent on

agriculture has actually increased between 1931 to 1951. Secondly, the density of population cannot be regarded as low for an agricultural country like India. Moreover, though the per capita income has shown a small increase over the decades, very few people would doubt the proposition that had the population of India grown at a smaller pace, the per capita income would have increased at a larger rate. The statement that India possesses large undeveloped resources is not relevant in this context. The real question is, given the present rate of development of the resources of the country, is India in a position to support a rise in population by about two per cent per year ? If the pace of development quickens in India, if her cultivators produce more food and other crops per acre of land, and her manufacturers and labourers turn out more goods in the factories and mines at a lower cost, India will no doubt be able to support a larger population on a rising standard of living. But this does not support the proposition that the present rate of growth of population is not excessive on the basis of the present rate of development of our resources.

There are many other indications of the existence of the pressure of population in the country. The comparatively high birth and death rates, widespread malnutrition and the existence of millions of people on a sub-human level,—these are all important indications. None of them is of course conclusive. But when all these evidences are studied together, very few economists will deny the existence of a serious pressure of population in our country.

Many British writers who argued that India was overpupulated seemed to imply that if only the growth of population was held in check in our country, all our problems would be solved. But this is not correct. Our economic problems would remain even if the growth of population was checked. At the other extreme, those who argued that India was not over-populated seemed to imply that if only the pace of economic development was quickened, the problem of population would be automatically solved. This is also a wrong proposition to take up. The task of ensuring a higher standard of living for the masses in India cannot be satisfactorily performed unless a simultaneous attack is launched on both fronts,—that of the development of resources and of the growth of population. We must recognise the truth of the proposition that a higher standard of living would be difficult of achievement unless the growth of population was checked along with the adoption of special measures for the development of our resources.

A Population Policy for India: It is wellknown that both the birth and death rates are comparatively high in our country. There are indications that economic development in the future is likely to

increase the pressure of population in the near future. As economic development proceeds, a large-majority of the people would enjoy higher standard of living, and have better food, housing and clothing and medical care. This is likely to accentuate the trend towards declining death rates. If, at the same time, the birth rate does not decline proportionately, population will tend to grow at a faster rate, putting a great strain on our resources. This has been the experience in Europe in the 19th century, where birth rates remained at a high level for three-quarters of a century even after a substantial decline in the death rate. The same thing is going to happen in India unless special steps are taken to control the birth rate. Europe did not suffer in spite of the accelerated rate of growth of population because its aggregate population was comparatively small when the industrial revolution began in that continent. The pace of economic development was quick, while the growth of population in absolute numbers (apart from percentages) was small. So Europe was able to enjoy a higher standard of living in spite of the growth of population in large percentages. Conditions are different in India at the present moment. She has already a very large population and a very low per capita income. The rate of capital formation is very low. The pace of economic development, which depends on capital formation, cannot be made quick enough to absorb the growing population and ensure a higher standard of living. Hence there is an imperative need for framing a positive population policy, aiming at a judicious control of the birth rate.

Family Planning: Any programme for ensuring a higher standard of living for the masses must, therefore, contain proposals for family limitation. The vicious circle of poverty and pressure of population can only be checked by a two-pronged drive—the adoption of a plan for economic development and control of the birth rate by various methods. Voluntary restraint on the part of married couples and late marriages will not slove the problem. It is only the positive birth control methods that will prove effective in checking the birth rate. Family limitation is also essential in order to secure better health for the mothers and better care and upbringing for the children.

There will, of course, be certain difficulties in regard to the adoption of a positive programme of family planning. The first is the extreme ignorance and conservatism of the masses. The second is their poverty. The masses do not possess the means of buying the birth control devices which are available in the market. The third is the danger to the future quality of the race. It has been urged that while the intelligent people will control birth, the ignorant and the weak will go on

multiplying at the same rate as before. So the number of intelligent and strong people may thus fall off in the next generation or two.

These difficulties point to the need of the state itself playing a considerable part in popularising different methods of family planning, such as, the oral fills, sterilisation operations, use of the loops. Attempts should be made to discover suitable methods of family planning and devise methods for securing a wide dissemination of the knowledge of these methods among the masses. All known devices of publicity—the press, the cinema, the radio etc., should be asked to carry on propaganda among the masses so as to make them conscious about the existence of the problem of population and to inform them about the merits of the various techniques of family planning. All government hospitals and public health agencies should have clinics where people can get proper advice on the most suitable method of family planning. The first five-year-plan has given emphasis on the need for family planning and allocated Rs. 50 lakhs to finance the nucleus of a family planning programme. In the 2nd and 3rd plans, the total allocation was raised to Rs. 5 crores and Rs. 27 crores respectively.

Progress in this direction has, however, been rather slow. Prof. Enke, an American economist, has argued in a recent paper that further expenditure on inducing the population to limit birth would be a better investment than the rupees spent on any other project. If by any such investment the birth rates can be kept lower, the smaller increase in population will result in a larger increase in per capita income. He even suggested the payment of a subsidy to those that agree to limit their families to a total. There is a good deal of substance in his contentions. There is no doubt that an effective family limitation programme must become a part of the economic plan.

Questions

1. Discuss the factors which determine the density of population in India. (Agra. 1936 ; Cal. 1935 ; Mad. 1938 ; Nag. 1939 ; Punj. 1938, 1951 ; Gau. 1952).

2. Is India over-populated ? If so, what remedies would you suggest to solve the problem ? (Ag. 1954 ; All. 1936 : Cal. 1942 Luck. 1957 ; Panj. 1939 ; Delhi 1958, 1952).

3. Do you agree with the view that the rapid growth of population in India stands in the way of economic progress ? Give reasons for your answer. (Del. 1953).

4. Bring out clearly the correct nature of the present population problem of India. In the light of your analysis, what should be the proper population policy for the country ? (Mad. 1953).

5. Make out a case for population control in India. (Kash. 1958).

6. Do you think that India is subject to increasing population and diminishing food at the present moment? (Punj. 1953).

7. "In India, there is really no problem of over-population at the present time." Examine this view. (Cal. 1938).

8. What are the factors which have accelerated the growth of population in India during the last two decades or so? What action is called for on the part of the State and the people? (I.A.S. 1954).

9. Discuss fully the effects of economic development on the growth of population in the present Indian context. (C. U. B.Com. 1958).

10. Why is Family Planning essential in India? Mention the main difficulties in its way and suggest measures to remove them. (Punj. 1957).

11. Examine the occupational distribution of population in India and explain its relationship with poverty in our country. (Raj. 1958).

12. "Viewed over a long period, the Indian Economy has been more or less stagnant and failed to meet the demands of a rapidly growing population."

Do you agree with the above statement? (Agra 1958).

"Economic development is not keeping pace with the increasing population in India". Discuss. (Utkal 1957).

CHAPTER 5 THE SOCIAL STRUCTURE AND THE ECONOMY

Man has always lived in society, and the social institutions exercise a profound influence over his activities. Hence in order to get a complete picture of the operations of the Indian economic system, it is necessary to study the socio-religious ideals and institutions which have been evolved in India.

The social organisation in India is characterised by the presence of two peculiar institutions, the caste system and the joint family system, both of which exercise some influence over the economic activities. In addition, notice should also be taken of the systems of inheritance prevalent in India and the religious ideals, all of which have some peculiarities of their own.

The Caste system: The most important characteristic of our social organisation is the existence of the caste system. It is one of the oldest institutions among the Hindus. A caste may be defined as consisting of a group of families bearing a common name, and generally following a specific occupation. The people of one caste must marry within the same caste and there are also restrictions regarding inter-dining with people belonging to other castes. Another peculiarity is that certain castes are regarded as high, while some castes are low or even untouchable. Birth determined one's caste irrevocable and people belonging to one caste must always remain in the same caste.

There are many speculations regarding the origin of this system, most of which are of no concern to us. Whatever its origin, there is no doubt that in the early societies, the system yielded some important advantages. By prohibiting marriage outside each group the system had enabled the Aryans to maintain the purity of their racial stock. Moreover, it exercised a stabilising influence in early societies. Under the operation of this system, men belonging to so many races who lived in India crystallised into different castes. Each caste had, therefore, its proper place in the social organisation, and soon learnt to live side by side in a spirit of fellowship. In addition to these sociological aspects, the caste system gives rise to some economic benefits. First, it enabled the society to secure the benefits of division of labour, as each caste specialised in one particular occupation. Secondly, one result of the caste system was the provision of an inexpensive and efficient method of training for the young apprentices. As the children follow the caste

profession they can learn everything about that particular occupation from their parents, and so have not to pay heavy premia in order to become an apprentice as is the practice in the western countries. The hereditary pursuit of occupations helped to preserve and increase the skill and dexterity of the workers. Thirdly, as the children know the profession they will follow, they escape the worries and uncertainties which the search for a career occasions. Lastly, the caste guilds performed many of the functions of the trade guilds of mediaeval Europe. They laid down suitable conditions for the practice of their professions, protected the interest of the members, and helped others who had fallen in distress.

The system has, however, given rise to grave evils which are hampering the economic progress of the country. Its greatest economic defect has been that it results in hindering the free mobility of labour. Under a rigid caste system, children must take up the caste profession. It is quite possible that the demand for the services of potters is declining. But a potter's children must follow in the footsteps of their father, even though the goods produced by their labour do not find ready buyers. In the opposite case, let us suppose that the demand for the services of potters increases considerably. Unless potters have more children, it will not be possible to increase the supply of potters. Unless one is born into a caste, one cannot adopt the profession special to that caste. As a result, mobility of labour becomes restricted and it becomes difficult to adjust the supply of different grades of labour to the changes in demand. Secondly, the principle of heredity, which forms the basis of the caste system, is also defective on another ground. There is no guarantee that a potter's son will also inherit the skill necessary for that profession, nor is there any certainty that he will like the potter's trade. He may, on the other hand, like to become a carpenter and may possess the necessary skill. But he cannot become a carpenter and must remain a potter. The caste system may, therefore, be responsible for many misfits in the economic organisation. Thirdly, the system has created a number of serious problems by dividing the society into water-tight, non-competing groups. The people who belong to the so-called higher castes generally possess a contempt for manual labour. They do not like to take up occupations which are supposed to be reserved for the so-called lower castes. The system is thus indirectly responsible to some extent for the middle class unemployment. The educated middle classes do not like to take up skilled jobs or occupations in trade and industry. They prefer the clerical or white-collar jobs as befitting their gentlemanly status. But these occupations are already over-crowded. Lastly, while the economic effects are thus bad, the political implications of the system are even

worse. The system is responsible for the existence of the problem of the depressed classes,—the so-called untouchables. It has meant a deplorable waste of the human talents and potentialities of the untouchables. It has created a great social cleavage between the different sections of the population.

The caste system in recent years: The impact of the western civilisation is slowly undermining the rigours of the caste system. The growth of communications and the construction of roads and railways have brought about an economic transition in India. The traditional village industries declined, and people have been forced by economic necessity to move out to the new cities and factory areas and to take up other occupations. Travel in railways has forced many people to give up some of the cherished caste rules. Urban life has resulted in the intermixing of various castes, many of which had to give up some of their rigid prohibitions. The spread of the liberal English education, and the attendance in the same class of pupils belonging to all castes, have all served to loosen the beliefs underlying the caste system. Many of the reformist movements among the Hindus have also disapproved of the caste system and insisted on inter-marriage among the different castes. While there is no doubt that all these forces have undermined the caste system, it is, however, questionable whether it will die out completely. The masses living in the villages still now cling to this system, and even the educated classes have not been able to free themselves completely of the prejudices of this system. But in spite of this, the economic defects of the caste system have been removed to a large extent. It no longer prevents the mobility of labour as people in large number have given up their caste professions and adopted other jobs.

The Joint family system: Another special characteristic of the Indian society which has some economic implications is the joint family system. In the west, a family usually consists of the man, his wife and unmarried children. When the son marries, he no longer lives with his parents. Not so in India. Here a family is joint in the sense that all brothers with their wives and children live together along with their parents, uncles and aunts. There is a common kitchen and common property.

The system possesses some advantages. In the first place, as many people live and eat togther, there is some saving in expenses. The expenses become less per head when many people live and dine together. Secondly, it tends to counteract the effects of the laws of succession. So long as the joint family system remained effective, the problem of sub-division and fragmentation of land did not become acute. Thirdly,

the system provided a good deal of social security to the people. The resources of all the members of the joint family helped to support the sick and the infirm, the unemployed and the old people. Members, therefore, enjoyed some protection against sickness, incapacity, unemployment and death. Lastly, the system tends to encourage the growth of the virtues of self-sacrifice, and cooperation among the family members. The members of the ideal joint family work on the principle of "each according to his need". They co-operate with each other and make suitable sacrifices to promote the interests of all members. These are desirable social virtues, and the system thus embodies many of the principles of a communistic society without its coercive nature.

But the economic implications of the system are not all beneficial. While the provision of security for all members against want, illness etc. is a desirable feature, it may have the unfortunate effect of encouraging idleness. When everybody knows that he can depend on the joint family, he may not exert himself. Thus the system may be responsible for the loss of initiative and enterprise. Secondly, in a joint family, members who earn a large income have to share it with others. So they may not be in a position to save large sums of money. As a result, the volume of savings becomes small and this hampers the growth of capital. Thirdly, when a man has to support a large number of members, as in a joint family, he may be afraid to take up risky enterprises. If these fail and he loses his money, so many people will be put to difficulties. So he may prefer to invest safely. Hence capital for investment in risky enterprises may not be forthcoming and the economic progress of the country suffers as a consequence. Moreover, the system tends to encourage conservatism and frowns upon individuality. The joint resources of the family are administered by the head of the family, who is usually the eldest male member. Old people are usually conservative in nature and discourage individuality among the younger members. Lastly, the system leads to frequent quarrels and much unhappiness. Members who earn more may grudge others who earn less or are idle. The peace and happiness of the family may thus be broken on many occasions by frequent quarrels born out of jealousies.

The system is, however, breaking down rapidly under the impact of economic forces. The influence of western education, the acute struggle for existence and the growth of individualistic spirit,—all these factors have combined to cause disintegration of the joint family system.

The Laws of inheritance: In the western countries, the eldest son usually inherits the property of the father. But in India, the laws of inheritance recognise a large number of heirs. Among the Hindus, under the Hindu Succession Act, 1956, the property of a Hindu who dies intestate is divided equally between his widow, his children and his grand children by a predeceased son or daughter. The mother of the deceased also inherits along with the children and the grand children. Under the Muslim law of inheritance, the property is divided among a large number of heirs, including sons, daughters and parents.

So the Indian laws of inheritance recognise a large number of heirs as against only one recognised by the western laws of succession. The Indian system has its merits and demerits. First, it has secured a wider distribution of property and so prevents great inequalities of wealth and income. Every son is assured of something to start with on the life's adventure, while none has enough so that he can stay idle. As each son's share is small, he has an added incentive to work hard in order to maintain his accustomed standard of living.

But the laws of inheritance have given rise to some economic evils. First, they have been responsible for the acute nature of the problems of sub-division and fragmentation of agricultural holdings. Secondly, they prevent large accumulations of capital by dividing property among a number of heirs. Lastly, as each heir is assured of a share in the father's property, he may feel no urge to work hard. As a result, the spirit of enterprise may be checked, leading to stagnation.

Religion and its economic impact: It has been stated by a number of western writers that the peculiar religious outlook of the Hindus is one of the most important causes of poverty in India. The Hindus have a fatalistic outlook on life and their religion teaches them to be otherworldly. But this is not correct. Poverty is not due to the fatalistic outlook of the people. On the contrary, it is extreme poverty which has bred fatalistic outlook among the people. The religious outlook of the Hindus is not the cause of their poverty. The Christian religion also preaches asceticism. In ancient days when the sway of religion was stronger than at present, the Indians amassed huge wealth, traded with the world and manufactured a large volume of goods. In fact, it was the wealth of Ind that attracted the foreigners to India in those days. Religion did not prevent the people from becoming rich in those days. The causes of Indian poverty must be sought elsewhere than in the religious outlook of the Indian people.

Questions

1. Describe the important features of the social structure of the people of India. Examine their influence on our economic life. (Cal. 1944 ; Punj. 1957, 1949 ; Ag. 1957 ; Del. 1951).

2. Discuss the economic implications of the caste system. What are the factors tending to break it up ? (All. 1933 ; Luck. 1956 ; Ag. 1954 ; Cal. 1933 ; Punj. 1943).

3. Consider the effect of the Indian joint family system upon the supply of enterprise and saving. (Cal. 1945 ; All. 1933 ; Del. 1933 ; Utkal 1956 ; Nag. 1939).

CHAPTER 6 NATIONAL INCOME OF INDIA

In the previous chapters we have discussed the resources in men and materials that are available for the development of our country. These provide the basic facts in a study of Indian economics. Our next task will be to determine the national income of India. Labour and capital of a country, working upon its natural resources, produce in every year a certain net aggregate of products and services. This is the national income of the country. Estimates of the national income and of its constituent parts serve a large variety of purposes. "They provide an index of economic activity and an instrument of economic planning. They show how incomes are earned and on what they are spent. They also show the distribution of income between classes. They can be used to measure the prosperity of one country with another or the prosperity of the same country at different stages in its history." If one knows the income of an individual, one can make a "rough guess as to his political opinions, his tastes and education, his age and even his life expectancy." Similarly, we can know a lot about the economic conditions of the people of a country if we have information about its national income and the actual distribution of that income.

Estimates of the National Income of India: Attempts have been made from time to time to estimate the per capita income in our country. These estimates formed before 1947 are given below.

TABLE 14

Name of the Person making the estimate	*Year or years for which the estimate is made*	*Per capita Income* Rs.	as	p
Dadabhai Naoroji	1867-70	20	0	0
Lord Cromer	1882	27	8	0
Digby	1895-99	17	8	5
Lord Curzon	1900	30	0	0
Wadia and Joshi	1913-14	44	5	0
Shah and Khambata	1900-14	36	0	0
Shirras	1921	107	0	0
Simon Commission	1929	116	0	0
V. K. R. V. Rao	1931-32	65	0	0

These are all rough estimates, as only in recent years some statistics which are necessary for the proper calculation of the national income are being published. Of these estimates, Dr. Rao's calculations may be considered to be to some extent reliable. Dr. Rao has criticised the statistics regarding agricultural production published by the government, and other data regarding mineral, industrial and forest produce, milk and milk products. He has supplemented them by reference to the income-tax statistics as well as figures of incomes of junior government servants and of the wages of industrial workers. These have further been supplemented by *ad hoc* enquiries.

Estimates of the National Income Committee: In view of the need for knowledge about the national income of our country, the Government of India appointed in 1949 the National Income Committee "to report on the National Income and related estimates, to suggest measures for improving the quality of the available data and for the collection of further essential statistics and to recommend ways and means of promoting research in the field of national income." The first report of the committee was published in April, 1951, and its final report has been submitted to the government in March, 1954.

In the first report, the Committee have sought to make an estimate of the national income for the year 1948-49. The total national income for that year has been estimated to amount to Rs. 8710 crores. Income from agricultural sources was estimated to be Rs. 4150 crores; from mining, manufacturing and hand trades Rs. 1,500 crores; from commerce and transport, Rs. 1,700 crores; and from other sources was Rs. 1,380 crores. In other words, agriculture, industries, commerce and transport and other services contributed 47·6 p.c., 17·2 p.c., 19·5 p.c. and 13·8 p.c. respectively to the total national income. The total income from these sources amounted to Rs. 8,730 crores from which Rs. 20 crores were to be deducted on account of the adverse balance of payments on income account. The resulting total was Rs. 8,710 crores. Since the aggregate population was estimated to be 341 crores, the per capita income came to Rs. 255 in 1948-49.

This estimate has been revised in the final report of the National Income Committee submitted to the Government in March 1954. The revised estimate placed the national income at Rs. 8,650 crores in 1948-49, and the per capita income at Rs. 246·9. Subsequent reports also gave details of national income for other years.

Table 15

Year		*National income (or net national output) at 1948-49 Prices*	*Per capita income at 1948-49 Prices*
		(Rs. crores)	Rs.
1948-49	..	8,650	249·6
1949-50	..	8,820	250·6
1950-51	..	8,850	247·5
1951-52	..	9,100	250·3
1952-53	..	9,460	255·7
1953-54	..	10,030	266·2
1954-55	..	10,280	267·8
1955-56	..	10,480	267·8
1956-57	..	11,000	275·6
1957-58	..	10,890	267·3
1958-59	..	11,650	280·1
1959-60	..	11,860	279·2
1960-61	..	12,750	293·2
1961-62	..	13,060	294·3
1962-63	..	13,310	293·4
1963-64	..	13,970	301·1
1964-65	..	15,050	317·0

The figures show a rise in the national income in real terms of 21·0 p.c. during the 5 years of the Second Five Year Plan period, (1956-57 to 1960-61), as against 18·4 p.c. rise in the national income over the First Plan period. During the 3rd Plan period, the national income has risen by only 12·7 p.c. The corresponding rise in *per capita* income, during the two periods, was 8·9 p.c. and 11·1 p.c. respectively. The per capita income remained more or less static during the 3rd Plan period.

Expressed at current prices, the national income stood at Rs. 20,010 crores in 1964-65 as against Rs. 14,800 crores in 1961-62, and Rs. 9,980 crores in 1955-56. The *per capita* income at current prices was Rs. 421·5 in 1964-65 and Rs. 333·6 in 1961-62.

The report also gives other interesting information. For example, small (largely household) enterprises contributed nearly 61·3 p.c. of the net domestic output, and large (generally joint-stock companies) enterprise produce about 12 p.c. of the net domestic output. Thus the relative importance of small enterprises is quite clear. Another interesting point

is that our foreign trade constitutes a comparatively small part of our national income. Exports and imports varied between 5 to 7·5 p.c. of the net national product excluding imports.)

Methods followed in estimating national income: Two methods are usually followed in calculating the national income of a country. According to the first method, an attempt is made to determine the sumtotal of income earned by the total working population of the country. This is the *income method,* which adds up the wages of workers, plus interest on loans and securities plus rents and royalties, plus corporate profits plus the net income of unincorporated business units. According to the second method, known as the *census of production or inventory method,* an attempt is made to find out the total net value of all goods and services produced in a given year.

The National Income Committee found that it was not possible to use either of these methods in India on account of the non-availability of data. We do not possess adequate statistics of total production in all industries, and the number of income tax payees are comparatively small in relation to the total population. Hence the committee have followed both these methods as and where statistics are available. "We have, therefore, estimated the total working force in 1948-49 and its distribution among different occupations ; this occupational classification is made on the basis of the classification of the economy by industry, including under the term, industry also agriculture, services and all other means of income generation. The inventory method is applied to as many sectors of the economy as possible, the value of net product being obtained by complicated process of estimation involving many ingenious devices and assumptions for inferring the magnitudes of the unknown from those of the known ; while for the remaining sectors the income method is applied, the number of workers in each category being obtained from the re-organised data on occupational classification."

Problems of national income estimation: The National Income Committee have pointed out a large number of pitfalls in framing a satisfactory estimate of national income. Even in advanced industrial countries with their wealth of statistics, estimators of national income have to face many problems. It is but natural that such problems would be somewhat greater in an under-developed country like India where adequate statistical data are not available on many sections of the economy.

In the first place, unlike the developed countries, a considerable portion of output produced in India does not come into the market, being either consumed by producers themselves or bartered for other

goods and services. This is specially true in the rural sector. The existence of a large non-monetised sector has greatly complicated the tasks of national income calculation. So in determining the amount and value of this part of the total output, one has to depend largely on pure guesswork, and this makes the calculations somewhat arbitrary.

Secondly, in Western countries statistics are largely collected from individuals and corporations. But the vast majority of the producers are illiterate, and neither they nor the consumers keep any accounts, or are in a position to keep accounts. Hence they are not able to supply the required data. Hence an element of guesswork therefore inevitably enters into the calculation of the value of output, especially in those sectors of the economy which are dominated by the small producers or household enterprises.

Thirdly, even with regard to the available data, they are subject to important limitations. The prices and expenses data for agricultural and related activities are quite incomplete. Information regarding industries is limited to only a part of those industries in which factory units are important. Data on total and working population were, until recently, incomepletely tabulated. Some of the items in the international balance of payments are still rough estimates. There are scarcely any data with regard to agriculture and related activities—no information on the structure of costs or on the saving and consumer expenditure of the rural population.

Finally, in view of the large regional diversities in India, inadequacy of data cannot easily be overcome by expanding data for one part of the country to the rest.

Hence the estimate of the national income of India is bound to be largely tentative. This is bound to be so until additional data are collected to fill the many gaps in our knowledge of the different sections of the economy. The committee have justified their estimates, however tentative they may be, on the ground that "the only way to make progress in this field is to make the best use of what is available and in the process point to the directions in which there is need for collection of additional data or for additional analysis."

National income by source: The National Income Committee have also published data relating to the major sources from which national income is derived in this country. The information is given in Table 16.

Table 16

NATIONAL INCOME BY SOURCE

(At Current Prices)

	1950-51	1955-56	1961-62
Agriculture & Allied pursuits	4,890 (51·3%)	4,520 (45·3%)	6,850 (46·8%)
Large Industry & Minerals	620 (6·5%)	880 (8·8%)	2,800 (19·1)
Small-scale Industry	910 (9·6%)	970 (9·7%)	
Railways & Communications	220 (2·3%)	300 (3·0%)	450 (3·1%)
Banking & Insurance	70 (0·7%)	90 (0·9%)	180 (1·2%)
Other Commerce & Transport	1,400 (14·7%)	1,490 (15·0%)	1,840 (12·6%)
Professions	470 (4·9%)	560 (5·6%)	790 (5·4%)
Administration	430 (4·5%)	570 (5·7%)	1,020 (7%)
Other Services	540 (5·7%)	600 (6·0%)	760 (5·2%)
Income from abroad	—20 (—0·2%)	..	—60 (—0·4%)
Total	9,530 (100)	9,980 (100·0)	14,630 (100·0)

Thus it is clear that the share of agriculture and allied pursuits, after a decline from 51·3 p.c. in 1950-51 to 45·3 p.c. in 1955-56, the last year of the First Plan, has risen to 48·3 p.c. in 1960-61, the last year of the Second Plan. It has again fallen to 46·8% in the provisional estimates for 1961-62. Thus the share of agriculture in the national income has declined by less than 5 p.c. over the last 10 years, while that of industries, large and small, has risen by about 15·5 p.c. Thus while industrial development is no doubt proceeding, the importance of agriculture still remains rather high, in spite of 10 years of economic development.

Growth in National Income: The Central Statistical organisation has published its estimates of national and per capita incomes on the basis of the rate of growth of population as shown in the census of 1961. The following table shows the relevant data.

Table 17

	National Income at 1948-49 Price (Base 1950-51=100)	Per Capita Income at 1948-49 Prices
1950-51	100	100
1955-56	118·4	108·2
1956-57	124·3	111·4
1957-58	123·0	111·7
1958-59	131·6	113·2
1959-60	134·0	112·7
1960-61	143·8	118·5
1961-62	147·6	118·9
1962-63	151·1	119·1
1963-64	157·3	121·4

This table shows in index numbers the rates of growth in both national and per capita incomes. Thus during the 13 years from 1950-51 national income has risen by 57·3 p.c., the growth during the First Plan period being by 18·4 p.c., and that during the second by 21·2 p.c. During the first 3 years of the 3rd Plan, national income has risen by only 13·5 p.c. The increase in per capita income over the whole period was 21·4 p.c., the average annual rate being 1·65 p.c.

This rate of growth in national income compares unfavourably with the growth rates in some other countries. Thus during the period 1950-59, the growth rate was 9·1 p.c. in Japan, 7·5 p.c. in W. Germany, 4·0 p.c. in France, 9·0 p.c. in Iraq, 6·0 p.c. in Philippines, 5·0 p.c. in Ghana as against 4·3 p.c. in India (1950-51 to 1960-61).

Questions

1. Write notes on the National Income of India. (Punj. 1953 ; Ag. 1956).

2. Discuss the difficulties in the way of a satisfactory estimation and analysis of national income in India. (W.B.C.S. 1952).

3. Give a brief account of the Report of the National Income Committee of India. (C.U. B.A. Hons. 1952).

4. Give an estimate of India's national income indicating the proportions derived from different sectors. How has the position changed during the Five Year Plans? (Del. 1959).

CHAPTER 7

AGRICULTURE—A GENERAL SURVEY

Agriculture and economic development: There is hardly any need to stress the importance of agriculture in the economic life of this country. According to the census of 1951, out of a total population of 35·6 crores, 24·9 crores (*i.e.*, 69·9 p.c.) depend mainly on agriculture for their livelihood. About 46·8 per cent of the total national income of India is derived from agriculture. India is the largest producer of sugarcane, tea and groundnut; the second largest producer of raw jute and rice and occupies the third place in respect of acreage among the wheat-producing countries of the world. Many of the raw materials required by her industries like jute, raw cotton etc., are the products of agriculture, and a large percentage of exports consists of agricultural commodities like tea, oil seeds etc. The Planning Commission have, therefore, rightly given topmost priority to the development of agriculture. Agriculture is the most basic and vital industry in our country.

Apart from this importance of agriculture in the Indian economy, it can be easily seen that the pace of economic development cannot proceed smoothly and rapidly unless agricultural development takes place simultaneously and probably at faster rates. As the income from agriculture constitutes more than 48 p.c. of the national income, the growth in the latter would be slowed down if the former did not increase at the same time. Moreover, economic development will by itself generate forces leading to considerable increases in the demand for agricultural crops. Economic development will bring about a rise in the money incomes of the people, and as their money incomes rise, people will spend a larger proportion of their incomes on foodgrains. The poorer the people, the larger is their expenditure on foodgrains of a simple kind, and in spite of this, a considerable proportion of these people is not in a position to satisfy even the minimum demand for foodgrains. So a rise in their incomes will induce them to buy more foodgrains. If, at the same time, the output of foodgrains is not increased in proportion to the rise in demand, foodprices will tend to rise, increasing the dangers of inflation. Workers would demand higher wages to compensate for the rise in their cost of living, thereby bringing about cost inflation. This would have adverse effects on the rate of economic development.

Increasing industrial development will also become difficult if agricultural output does not rise in the meantime. The rate of growth

in such industries as are based on agricultural raw materials (such as jute or cotton or oilseeds) would slow down if the production of these crops could not be increased in proportion to the rise in demand. If the production of raw materials lags behind, these would have to be imported from other countries if the growth of these industries was to be maintained. But the lack of foreign exchange resources would make it extremely difficult, if not possible, to increase their imports. Moreover, about 70 p.c. of the people of this country depend on agriculture for their livelihood, and their incomes depend on the rate of development of agriculture. If agricultural development lags behind, and so the incomes of the vast majority of the people do not rise proportionately, they would not be able to buy the output from industries. If the market for the manufactured goods thus becomes narrow, the rate of development of industries would per force slow down.

There is another way in which the development of the two would be found to be inter-linked. A faster rate of growth of industries cannot be achieved at present unless we can import the necessary capital goods from other countries. As our foreign exchange resources are limited, we would not be able to increase our imports of capital goods unless we could increase our exports. A large proportion of our traditional exports consists either of agricultural goods, or of goods produced with agricultural raw materials. A high rate of increase in agricultural production is, therefore, a pre-requiste for increasing our exports, and so our imports of capital goods.

Thus the development of agriculture and that of the economy in general are inter-linked together. In fact, if we analyse the history of economic development in a number of advanced countries, we shall find that the generation of agricultural surpluses had considerably facilitated and hastened the growth of industries and of the economy as a whole. As agriculture yielded or was forced to yield a considerable surplus of output over consumption, the consequent saving was utilised to increase the rate of capital formation in the country.

Lastly, a faster rate of development in other sectors of the economy is also essential to agricultural progress. A very large population is now dependent on land and this acting as a drag on agricultural development. In so far as the development of other sectors provides more employment and so draws off people from land, this would facilitate the adoption of improved methods of cultivation.

Characteristics of agriculture: Since agriculture is the most basic industry, it is necessary to study its principal characteristics. The first characteristic is that agriculture is carried on mainly on the basis of subsistence farming. In other words, the cultivators till their land mainly to provide the essential requirements of their family. Only the surplus that remains after meeting the family's consumption needs is sold in the market. This is to be contrasted with commercialised agriculture, where the crops are grown mainly for sale in the markets, only a small portion being retained for family consumption. Agriculture in India is mainly "a way of life", to be pursued from generation to generation.

A second characteristic is the progressive sub-division and fragmentation of land. Due to a variety of reasons of which the laws of inheritance and the absence of alternative occupations in the rural areas are the most important, agricultural holdings are being sub-divided into smaller plots with each passing generation.

Thirdly, the methods of cultivation are notoriously old-fashioned. The cultivators are still ploughing their land with the ancient plough, driven in most cases by weak and hungry bullock. They grow the same kind of crops in the same traditional manner. Cultivation on modern scientific principles with uptodate appliances is more or less an exception.

Another characteristic is that as a profession, agriculture is considerably overcrowded. Too many people depend upon land for their livelihood. Whole more than 69 per cent of the total population of India are employed in agriculture, about 19 p.c. of the population are so employed in the U.S.A., South Africa and Holland, 10 p.c. in Australia, 20 p.c. in New Zealand and 29 p.c. in Western Germany. This pressure of population is responsible for the extensive subdivision and fragmentation of holdings.

While the number of people dependent upon land has been increasing, the net area sown has not materially increased except in U.P. The total cropped area has lagged far behind the growth of population. In spite of this pressure of population, very little expansion of cultivation to waste lands has taken place. This seems to indicate that the available cultivable waste lands do not generally lend themselves to reclamation within the present resources of the cultivators.

Lastly, the yield of crops per acre of land is extremely low. This will be evident from Table 18.

Table 18

Yield per acre in some countries

Rice	India	690 lbs	(1949-50)
	Burma	1216 lbs	(1948)
	China	2243 lbs	
	Japan	3321 lbs	
Wheat	India	585 lbs	(1949-50)
	Australia	909 lbs	(1948)
	U.S.A.	1079 lbs	
Cotton	India	72 lbs	(1949-50)
	Egypt	590 lbs	(1948)
	U.S.A.	312 lbs	
Sugar (Raw)	India	3049 lbs	(1949-50)
	Cuba	4567 lbs	(1948)
	Mauritius	6132 lbs	

Not only is the average yield extremely low as compared to that of other countries, but a matter for serious consideration is that, according to the official estimates, during the 15 years between 1936 and 1951, there has taken place a decline in the average yield per acre in respect to the principal crops.

Table 19

Average yield per acre (in pounds)

	1951	1936
Rice	809	632
Wheat	629	556
Sugarcane	3,046	2,794

The result of all these factors is that the average income in agriculture is well below the general averages in the country. As the income from agricultural operations is less than 50 p.c. of the total national income and about 70 p.c. of the population lives by agriculture, this means that the per capita income of the agricultural classes is roughly $^3/_7$th of that of the non-agricultural classes. The typical unit in Indian agriculture is a very small farm which operates with very little

capital of any kind, the biggest items being the plot of land and the livestock. The extent of modernisation is practically insignificant.

Low productivity in agriculture: One of the most distressing facts about Indian agriculture is the extremely low yield per acre. The average yield per acre of almost all crops is lower in India than that in any other advanced country of the world. What are the causes of such low productivity? In other words, what are the main defects in the agricultural organisation of India? The main defects in Indian agriculture are the small size of the farms, primitive methods of cultivation, lack of water and manure, use of inferior seeds and ancient implements, and the defective system of land tenure.

The average size of farms in India is very small and is getting smaller with the passing of generations. While the average size of an agricultural farm is only 5 acres in India, it is 145 acres in the U.S.A., and about 40 acres in Denmark. The small size is due to the growing pressure of population and to the lack of any alternative sources of occupation for the rural people. This is a fundamental defect in our agricultural organisation. When farms are of such a small size, it will not be possible for the cultivators to use modern appliances.

A second defect is the prevalence of primitive methods of cultivation. The cultivators are still using the ancient plough, which merely scratches the surface. The use of agricultural machineries like tractors etc., which has led to a vast increase in productivity is practically unknown in our country. The cultivators, being mostly illiterate, know nothing of the scientific methods of cultivation; and being extremely poor, they cannot afford to buy these machineries even if they come to know of them. On account of their ignorance and poverty, the cultivators are not careful about the kind of seeds they use. The use of inferior seeds leads to low output.

The poverty of the cultivators is also responsible for another defect. The fertility of land has deteriorated to some extent on account of continuous cropping without manures. The cultivators are too poor to buy the artificial fertilisers in sufficient quantities. Cowdung is used as fuel, while their prejudices stand in the way of the use of bones, night soils etc. as manures. As a result, fertility of land is declining.

The soil in India is dry and will not yield good crops unless water is applied in sufficient quantities. But the supply of water is inadequate. Only 17 per cent of the total sown area is irrigated, while the remaining land has to depend upon the monsoons for the supply of water. But the monsoons are uncertain and irregular and all parts of the country

do not always get proper rainfall. The consequent lack of water is one of the most important defects of agriculture.

The systems of land tenure which were prevalent until recently do not leave the cultivators with sufficient incentive to improve the cultivation of land. The majority of the actual cultivators are tenants and have to pay high rent to their landlords. Hence they do not feel that they have any stake in land and do not exert themselves to improve cultivation.

The Indian cultivator is no doubt as hard-working as the farmer of any other country. He is also shrewd and intelligent. But he is, as a rule, illiterate, and so he has no knowledge of modern methods of cultivation.

There are also other defects in the agricultural organisation. Finance is the life-blood of every organisation and the supply of finance is inadequate in the rural areas. Cultivators are extremely poor and so are forced to depend on outside sources of finance (mostly money-lenders) for meeting their essential needs. As a result, most of them are heavily involved in debts and cannot afford to spend money for making improvements in land. They have to pay interest at very high rates on these loans, and this eats up a very large slice of their already small incomes.

Lack of finance is also responsible for another defect in the agricultural organisation. As most of the cultivators are heavily indebted to the mahajans, they are often obliged to sell their produce to the latter at reduced prices. Or, they have to sell in the market immediately after the harvest when the prices of crops are usually the lowest, in order to meet the demand of the mahajans for repayment. The marketing organisation is also defective in many respects. There is a long chain of middlemen and dealers between the cultivator and the final consumer, and they take away a considerable percentage of the price of the crops. Out of every rupee paid by the consumers, the cultivators usually receive about 8 to 9 annas, the rest being pocketed by those middlemen.

Lastly, there is an absence of suitable alternative sources of occupation for the cultivators. It is well-known that agriculture is a seasonal occupation, occupying the time of the cultivators for 4 to 6 months. For the rest of the year they have to remain idle. In old days they spent their spare time in carrying on one or other of the cottage industries. But most of these industries are in a decaying condition.

Remedies for the defects of agriculture: The outstanding fact about Indian agriculture is the extremely low yield from land. Not only is the yield low, but there is the evidence that it has not increased by any significant extent over the last decades. On the other hand, the population of the country has been increasing by large numbers. So unless steps are taken to increase the yield, India would have to face great difficulties in supporting the huge population.

The low yield is due to a variety of factors, *e.g.*, the uneconomic size of the holdings ; inadequate supply of water, primitive methods of cultivation, lack of capital leading to the inability to use good seeds or manures, defective marketing organisation, ignorance and ill health of the cultivators and defetive systems of land tenure etc. The remedies must seek to remove those defects.

First of all, steps should be taken to increase the size of holdings, either by the methods of compulsory reconstitution of holdings, or by the adaptation of co-operative farming or on the Soviet model of collective farming. As these steps might result in unemployment among the agriculturists, new employment must be found for them either in the villages by the development of cottage or small-scale industries, or in the towns by the establishment of industries.

The next important reform should deal with the systems of land tenure. The Zemindari system has rightly been abolished and means must be found to establish direct relationship between the cultivators and the government, while providing sufficient incentive to the former to improve their land.

Thirdly, we must look to the soil. Steps should be taken to prevent the erosion of the soil by means of afforestation etc. Better provisions for irrigation must be made by the construction of irrigation canals, tubewells etc, More manure should be applied to the soil. The Agricultural Departments should conduct research and devise improvements, better qualities of seeds, better control of pests and diseases etc., and find out ways of supplying them to the cultivators at reasonable cost. The government should build up an organisation to distribute seeds among the cultivators, and to familiarise them with the use of better types of implements.

Fourthly, another necessity is to improve the organisation for the supply of finance to the cultivators. The best way to do that is by encouraging the co-operative method in various directions. Methods of marketing must also be improved by the elimination of unnecessary middlemen, prevention of fraud and adulteration etc. For this purpose, steps should be taken to organise multipurpose co-operative societies

which should look after marketing, supply of good seeds, manures, purchase of cattle and improved implements etc. The present co-operative organisation should be re-vitalised.

But the most essential reform is the spread of education in the villages. The education should aim at providing not only knowledge of the three R's, but knowledge of improved methods of cultivation. Only through the spread of education it will be possible to secure modernisation of agricultural technique. It is also essential to take all possible steps to infuse new life into the villages. As the First Five Year Plan notes,—"The peasant's life is not cut into segments in the way the Government's activities are apt to be ; the approach to the villager has, therefore, to be a co-ordinated one and has to comprehend his whole life." It will not be enough if only certain economic reforms are brought about in the agricultural organisation. To have a lasting improvement, steps must also be taken to bring about a number of changes in the social and religious life, habits and customs of the rural population.

The question of mechanisation in agriculture: The need for increased agricultural output is admitted on all hands. A number of writers have, therefore, expressed their opinion that steps should be taken to mechanise agriculture in our country. It is well-known that in the western countries, the introduction of various types of machines like tractors has increased the yield of crops from land enormously. If such machines are adopted by our cultivators, the output of crops per acre will improve by a large percentage. Moreover, certain parts of land classified as "culturable waste" can be brought under cultivation by the use of tractors and other machines.

The use of machines in agricultural operations has made notable progress in many of the western countries. In France and Denmark farms use many kinds of agricultural machinery including the harvest-binders and reapers which can be found extensively even in small farms. In the wheat-growing areas of the U.S.A., almost all firms use tractors and other implements. In the U.S.S.R. the government have encouraged and forced the adoption of mechanised cultivation on an unprecedented scale both before and after the second world war. There is no doubt that the result of such mechanisation in agriculture has been beneficial. It has enabled the cultivators of these countries to produce more, and to enjoy a high standard of life on the farm with more leisure.

Attempts have already been made in India to introduce machines in the cultivation of land. Following the recommendation of the Food Grains Policy Committee, steps have been taken to bring culturable

waste land under cultivation with the use of tractors in U.P., M.P., Punjab, Madras and Bombay. The Government of India obtained about 300 surplus tractors from the U.S.A. stores after the second world war and with these as nucleus, a Central Tractor Organisation of the Ministry of Food and Agriculture has been set up. Considerable areas of waste land have been reclaimed with the use of these tractors in Khurai in M.P., Ganga Khadar, Nainital Tarai and Jhansi in U.P., and in the districts of Hissar, Rohtak, Ludhiana, Jullundur, and Ambala in Punjab.

The desirability of mechanisation in agriculture has been questioned by a large number of writers. Such mechanisation, it has been urged, is neither possible nor desirable in our country. It is not possible because of several factors. The first is the extremely small size of agricultural holdings in India. In order that a tractor can be worked economically, it is necessary to have a plot of land consisting of at least 100 acres. But only a very small number of farms in India is of this size. Secondly, the average cultivator is so poor that he cannot afford to buy modern agricultural equipment which is expensive. Moreover, the conditions of the soil in India are different from those in the western countries and tractors of the type in use in these countries, are not suitable for our country. Lastly, the wide use of machinery in cultivation has been made possible in the western countries because of the extension of electricity to the rural areas, the manufacture of machines suitable to farms in varying conditions of climate and geographical factors, and the spread of technical and rural engineering instruction to the villages. Almost all these factors are absent in our country. Electricity has been brought to only a few villages. The villages do not also possess good repairing organisations without which the extensive use of machines will be impossible. There is also a lack of technical personnel to repair these machines in the villages.

Thus while the possibility of a rapid mechanisation of agriculture is extremely doubtful, its desirability is also not obvious. Mechanisation, if carried on at a rapid pace, will throw large numbers of the rural workers out of employment. Already the incidence of unemployment and under-employment is very high in our agricultural organisation. Mechanisation will, therefore, give rise to serious problems.

There are also many other difficulties in the way of rapid mechanisation. The small size of holdings, the innumerable tenurial patterns, the poverty and illiteracy of the cultivators,—these will certainly limit the pace of mechanisation. But the need for the wide use of machines cannot be denied, especially for the reclamation and cultivation of large areas of waste lands. In all other countries mechanisation has

been regarded as a boon to society. It has increased the yield from land and ensured higher wages for labour, and higher incomes for the farmers who have thus been enabled to lead a happy farm life with increased leisure.

Questions

1. What are the main problems of Indian agriculture ? How is it proposed to solve them during the next five years ? (Punj. 1953 ; Cal. 1939).

2. "The central problem in planning and development of India's economy is the reconstitution of agriculture." Discuss. (Bom. 1953).

3. Would you like to have mechanised agriculture in India ? Explain clearly its possibilities and drawbacks in a country like India. (Cal. 1951).

4. Discuss the importance of agriculture in India's economic development.

CHAPTER 8 THE SIZE OF HOLDINGS

One of the most important causes of the low agricultural productivity in our country is the extremely small size of the unit of cultivation. The problem is of two-fold character. First, the size of a holding (*i.e.* the area cultivated by a person or a family) is small. Secondly, even these small holdings are seldom found in one compact bloc. They are scattered all over the village in still smaller plots. The first is the problem of sub-division of holdings, the second is known as fragmentation of holdings.

Sub-division of holdings : There is no doubt about the fact that in India the unit of cultivation is probably the smallest in the world, and it is getting smaller with each passing generation. According to the figures published in the First Five Year Plan, the vast majority of the holdings is on the average less than 5 acres. Holdings containing upto five acres of land constitute 83·3 p.c. of the total holdings in Bihar, 81·2 p.c. in U.P., 74 p.c. in Orissa, 66·1 p.c. in Assam and 52·3 p.c. in Bombay. In Madras, holdings assessed upto Rs. 10 or less constitute 82·2 p.c. of the total holdings.

A recent NSS survey of landholdings shows that 22 p.c. of the households in the rural areas own no land, about 25 p.c. of these households own less than one acre of land. Another 27 p.c. possess less than 5 acres of land per household. They constitute nearly three-fourth of the rural households and own only about 18 p.c. of the land in the villages. Another 13 p.c. own 5 to 10 acres of land, and the rest (*i.e.*, 18 p.c.) possess 10 or more acres.

The average size is thus very small as compared to the averages in other countries. For example, in other countries, the average size of holdings is about 27 acres in the U.K., 15·5 acres in France and 140 acres in the U.S.A.

Fragmentation of holdings : A greater evil than sub-division is the growing fragmentation of holdings. Not only is the average size of holdings very small, but even this small unit of holding is not situated in one compact bloc. Most of these holdings have further been divided into small plots which lie scattered in different parts of a village or in different villages. It has been found in a Punjab village

that the land has been divided into 1898 fields averaging one-fifth of an acre. In another village 12800 acres have been found scattered in 6300 fields. The average size of plots was found to vary between ·28 acres and ·81 acres. In Bombay and Assam, each holding consisted of an average of 3·3 to 4·5 plots of land.

Evils of sub-division and fragmentation : The small size of the unit of cultivation in India is possibly the biggest single factor causing low productivity. First, the small size has meant small output, higher costs and lower money incomes. It makes the use of machineries and other labour saving devices unprofitable. It creates difficulties for irrigating the plots. The small size of the holdings and the scattered position of the plots make it uneconomic for the cultivator to sink a well. It may not be within the financial capacity of the cultivators. Moreover, it may prove difficult for the cultivators to watch the crops on the scattered plots, and they may find it impossible to pay proper and timely attention to all plots of land situated in different parts of the village. Secondly, sub-division and fragmentation of holdings also involve a huge waste of land, time and energy. Large areas of land are lost in boundary lines and hedges. Much time is also lost in going from one plot of land to another. They are a fruitful source of enmity and litigation between neighbours who accuse each other of encroaching upon their own plots of land, or who may dispute each other's rights of passage over the plots of land. Thirdly, as the plots are small and scattered, it is not possible for their owners to build hedges round each plot or to fence them properly. So the crops growing on these plots cannot be effectively protected against the ravages of unwanted cattle and other animals. Lastly, the small size of holdings means that their owers can furnish only small security. So they have to pay high rates of interest when they borrow. The burden of interest payments has, as a consequence, grown very heavy. Thus sub division and fragmentation have checked improvement, resulted in considerable wastage of human, animal and material resources, increased the cost of production and have even thrown some plots of land out of cultivation in many areas. As the plots grow smaller and smaller in size, it may no longer be profitable to cultivate some of them. When the plots are scattered, the cultivator may not find the time to cultivate all of them.

It should, however, be mentioned that there are some writers who find some merits in the fragmentation of holdings. According to them,

the system of fragmentation enables a large number of cultivators to have a share of the more fertile land in the village, or to have plots of land of differing soil conditions. This is an advantage as it reduces for each farmer the risks and uncertainties of cultivation.

Causes of sub-division and fragmentation : The main causes of sub-division of holdings are the growing pressure of population on land and the difficulty of providing alternative occupations. As is well-known, the population of India has been growing at the rate of more than one per cent per year over the last 50 years. But the area under cultivation has not increased proportionately. On the other hand, the village industries declined one by one, while employment in modern, large-scale industries increased at a very slow rate. As a result, the growing population had to fall back on the land for their livelihood. These tendencies have been accentuated by the laws of succession which provided for the equal division of the property among all the heirs. So long as the joint family system was prevalent, the brothers cultivated the plots jointly, and the problem thus did not grow acute. But with the decline of the joint family system, cultivation is no longer carried on jointly, and this has increased the magnitude of the problem. Fragmentation of holdings is due primarily to a desire to secure equal shares for all heirs. If the father died, leaving two sons and two plots of land, of unequal fertility, the sons got shares in each plot of land.

Remedies : The remedies that have been proposed or attempted can be classified into five groups, *viz.*, consolidation of holdings, reconstitution of plots into economic holdings, collective farms, co-operative farming and co-operative village management.

(1) Consolidation of holdings : Some attempts have been made in this country to secure consolidation of holdings by various methods. This has been done in three different ways. First, it was sought to consolidate the small, scattered plots into bigger units by voluntary methods. The government officers tried to persuade the cultivators to agree to consolidate their holdings by the offer of some concessions. To facilitate such transactions the Baroda Government passed an Act in 1920. In Punjab, and to some extent in P.P., while no specific legislation was passed, attempts have successfully been made to consolidate holdings by forming co-operative societies.

By 1950, about $2\frac{1}{4}$ million acres in Punjab, 7500 acres in U.P., and half a million acres in Madhya Pradesh have been consolidated. In Bombay, a total are of $6\frac{1}{2}$ million acres has been consolidated. While co-operative consolidation has thus made some progress, it was felt that the pace of consolidation under the voluntary method was bound to be very slow. Hence the different States sought to introduce some element of compulsion for hastening the work of consolidation. This element of compulsion was introduced in two stages. In the first stage, the initiative in consolidation came from the local people. If a majority or a certain percentage of the owners or cultivators agreed to accept the scheme, the minority was to be forced by law to accept it. The C.P. Consolidation of Holdings Act of 1923 was of this type. Under that Act, if not less than one-half of the permanent holders, holding not less than two-thirds of the cultivated area, agreed to accept a scheme of consolidation, it would be binding on all holders. The Punjab and the U.P. Government also passed similar legislation. Though some action had been undertaken under these Acts, the results have not been satisfactory. They were applied very cautiously and as the initiative in consolidation was to come from the people, progress was also slow.

In the third stage, the element of compulsion was further increased. The initiative in framing a scheme of consolidation is to be taken by the State Government, which can enforce the scheme on all holders, irrespective of their consent. The Bombay Prevention of Fragmentation and Consolidation of Holdings Act of 1947 authorised the government to frame and enforce a scheme of consolidation in a particular area. A similar Act has also been passed in Punjab in 1948, under which consolidation proceedings can be started either by the government on its own initiative, or on the application of the owners of land. The U.P. Government has also passed a similar Act, the U.P. Consolidation of Holdings Act in 1953. Recent legislation has also sought to incorporate measure to prevent the future recurrence of sub-division and fragmentation. Both the Bombay and the Punjab Acts, cited above, contain provisions to that effect and in U.P., the Zemindari Abolition placed restriction on future partition of holdings.*

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* For a summary of legislation see Agricultural Legislation in India. Vol. II (Ministry of Agriculture, Government of India). See also "Consolidation of Holdings in India" *R. B. Bulletin.* June 1963.

In spite of these laws, the progress of consolidation has been most uneven. Two States, Madras and Kerala, have yet to pass this type of legislation. In about 4 or 5 States including Assam, Orissa, and West Bengal, these laws, though passed, have not been implemented or the rate of implementation has been very slow. The Third Plan proposed that about 30 million acres would be consolidated, and it is likely that this target might be achieved by the end of the year, 1965-66. Even then the progress would not be very large in comparison to the total acreage of the country, and the imperative needs of increased agricultural output.

(2) **Economic holdings :** A proposal, popular with many economists, is the reconstitution of the scattered holdings into what is called "economic holding." An economic holding consists of that area of land, the cultivation of which enables a family of farmers to enjoy a reasonable standard of living without help from outside sources. It is quite obvious that the size of such holdings would vary in different localities according to the character of the soil, rainfall, facilities for irrigation etc. Estimates of the size of an economic holding vary from 4 to 6 acres to 40 acres of land. The U.P. Zemindari Abolition Committee of 1946 thought that an economic holding should consist of 10 acres, while the Agrarian Reforms Commission of Saurashtra of 1951 expressed its opinion in favour of an area varying between 25 to 40 acres. The Congress Agrarian Reforms Committee, while correctly defining an economic holding, held, however, that in our country holdings of a smaller size (*i.e.*, smaller than the size of an economic holding) should be the ideal on sociological grounds. Such holdings have been called basic holdings.

This method proceeds to solve the problem in the following way: First, an enquiry should be held in different localities to determine the size of an economic or basic holding. After this is done, attempts are to be made to reconstitute all holdings on the basis of economic holdings by persuasion or compulsion. The law should also prohibit any sub-division of such holdings.

Nothing substantial has been done with regard to the operation of this proposal. The Bombay Prevention of Fragmentation and Consolidation Act of 1947 contains provisions under which the State Government has the power to fix and determine, in relation to any local area and the class of land, the size of holdings that can be cultivated

profitably as a separate plot. This extent of land is to be called a "Standard area". Any part of the land below this area is defined as a fragment. Any transfer or partition of land which will create a fragment is prohibited. The Punjab Act of 1948 also contains similar provisions.

There are two great difficulties in regard to this proposal. First, the determination of an economic holding in different localities will not be an easy or inexpensive task in view of the extremely divergent conditions prevailing in the country. Secondly, reconstitution of existing holdings into economic holdings would result in throwing a large number of people out of land. It will create huge rural unemployment and the consequent social disorganisation.

(3) Collective Farming : One way to solve the problem may be to follow the Russian model, and form collective farms by abolishing private ownership in land. That collective farms have increased the productivity of Soviet agriculture may be readily admitted. But the adoption of this proposal would be unjust only with regard to land if at the same time, other forms of property are left under private ownership. Unless private property is abolished everywhere the proposal is not likely to find acceptance in the country.

(4) Co-operative Farming*: Under this system, the cultivators and the owners of the different plots in a village or villages form a co-operative farming society. They pool all their land together, cultivate it jointly and then divide the produce according to some pre-arranged basis. The main advantage of this method is that while nobody is dispossessed from land, large-scale farming can be undertaken. Such co-operative farming provides the best solution for the problems of sub-division and fragmentation. Co-operative farming may be of four different types, co-operative joint-farming, co-operative tenant farming, co-operative better farming and co-operative collective farming. *A co-operative joint farming society is formed by a number of small owners.* The plots owned by them are pooled into one unit. Cultivation and management are carried on jointly by all members, who retain ownership over their plots. The members are paid for their work and any profits are distributed among them. *A co-operative tenant farming society does not undertake cultivation.* It divides the land it owns into

* See the note at the end of this chapter.

blocs which are then let out to cultivators for rent. These cultivators enjoy certain privileges regarding seed, implements, manures etc., from the society, and have to cultivate the land according to the plan laid down by the society. These societies are suitable at places where new land is being brought under cultivation. *A co-operative better-farming society* is formed to improve agriculture, not to secure large-scale cultivation. The society supplies better seeds, manures, implements etc., to the members, and provides for the marketing of their produce. *A co-operative collective farming society* itself owns or leases the land, and carries on cultivation. Members receive wages for their work, and may be paid a dividend in proportion to their wages. A number of farming societies have already been formed in different States in India For example, in Bombay, these societies were started as early as 1921. But they gained momentum only after 1949. At the end of 1949-50, Bombay had 79 co-operative farming socities, which cultivated an area of about 11,750 acres. Attempts at co-operative farming are also being made in Assam, Behar, Orissa, M.P., Mysore and other States. Most of them are, however, in an experimental stage. In U.P., experiments in the formation of these societies were conducted in two villages in the Jhanshi district. The entire management, cultivation, harvesting and disposal of produce was done jointly by the members through their Panchayats. These societies are being organised mostly when settling cultivators on new lands, supplied by the government. The U.P. Zemindari Abolition and Land Reforms Act of 1951, the Hyderabad Tenancy Act and the Bombay Tenancy Act have made special provisions for encouraging co-operative farming. The U.P., and Hyderabad Acts make it compulsory for all cultivators to join a co-operative farm if two-thirds of the right-holders covering not less than two-thirds of the area agree to form such a society.

The principal difficulty experienced in organising these societies is that the farmers do not readily respond to co-operative effort. Cultivators have been found to be lacking the spirit of self-help, mutual trust and leadership which is essential for the effective working of these societies. Hence it is being increasingly felt that some degree of compulsion may be necessary to pool the land and ensure cultivation by co-operative methods. That has been the opinion of the Congress Agrarian Reforms Committee.

(5). **Co-operative or joint village management :** The Planning Commission has recommended this method as a solution of the problem of sub-division. The central idea is to evolve a joint organisation of both the owners and the tillers of land which shall supervise the cultivation of the land. All plots are to be cultivated jointly and the crops raised on all land are to be divided among the owners and the actual cultivators in the form of ownership dividends and wages. The managing body of this organisation is to consist of the representatives of all the families in the village. Its main function will be to divide the work of cultivation among the working members and to distribute dividends.

Such an organisation may be utilised to carry out an all-round improvement in the social and economic life of the village. It may be organised on the co-operative basis, or merely as a joint body of the villagers. There is no doubt that this has great possibilities. But there has to be a great deal of trial and experiment before the most suitable pattern of such an organisation may be evolved. There is no doubt that something along these lines, or on the pattern of co-operative joint farming is to be preferred to the method of forced consolidation of holdings. There are obvious disadvantages in the latter method of converting small plots into large holdings. It would result in the conversion of owners of tenants of land into hired workers on large farms. Self-employment and rural unemployment will appear undisguisedly as an absolute lack of work and income. One should, as Dr. Datta has warned us, "remember the result of the enclosure movement in Britain which created a surplus population of 'semi-employed, inefficient labour' troubling the government and local authorities for many decades"* before coming to a final decision on the proper solution of this problem.

A note on co-operative farming

It has long been felt that the problem of sub-division and fragmentation of holding can be best solved through the introduction of the system of co-operative farming. The principal advantage of such farming is that it enables us to secure the advantages of large-scale cultivation without displacing any owners from their small holdings. There will then be no necessity for a large-scale displacement of men

* B. Datta. *The Economics of Industrialisation* p. 124.

from the rural areas, as is bound to be the case if the small plots of land are to be consolidated into economic holdings. The latter is not a practicable proposition so long as new industries and other non-agricultural occupations are not made available in the rural areas to absorb the men thrown out of land. The land reform proposals in every State envisage the fixing of a ceiling on individuals land holdings, and this would result in the breaking up of large cultivation-units into small ones. As this may result in increasing the inefficiency of agricultural operations, the Planning Commission have recommended the widesspread adoption of the system of co-operative farming in this country. Recently the majority of the members of a Delegation sent by the Government of India to China have advocated the adoption of co-operative farming, while a minority have expressed its strong opinion against such a measure. At its Nagpur session, the Congress have adopted the method of co-operative farming as the main plank in the reorganisation of agriculture.

By the end of 1958, there were about 2020 co-operative farms, the largest number being in Punjab (478), followed by Bombay (402). U.P. (255). Assam (170), W. Bengal (148).

The general argument in favour of co-operative farming is that it will provide the means for bringing the benefits of large-scale operations to small cultivators. Improved methods of cultivation as better seeds, fertilizers, improved crop rotation, effective plant protection etc. can be promoted only very slowly, if small cultivators, especially the illiterate ones, are to be approached individually. The rate of progress would be quicker if cultivators are united into co-operative farming units. It will then be possible to combine modern techniques with small holdings.

There is, however, a large section of opinion which sees no special merit in the system of co-operative farming. These people point attention to the psychological and other difficulties of working the system of co-operative farms. As voluntariness has to be the basic principle of co-operative farming, we have to consider at first whether the mentality of the cultivators is of such a nature that they would show the relatively high degree of co-operation needed for co-operative farming. The fundamental weakness of the system of co-operative farming lies in the fact that such a co-operative farm would have to distribute the crops

either on the principle of the need of each cultivator or on that of the amount of work performed by each of them. If the first principle is adopted, there would be a lack of incentive to work hard and so efficiency would suffer. If the share of each cultivator is to be determined on the basis of his contribution in land and labour, disputes are bound to arise regarding the relative intensity of work by different members. Common village rivalries and factions, and the difficulties involved in assessing the quality of land and the intensity of labour in agricultural operations are bound to hinder the successful working of such farms. Secondly, there is no evidence to prove that co-operatve farming, by itself, will increase the productivity of agriculture. Under normal economic and psychological conditions and without outside help co-operative farming has not proved its superiority as compared with the system of individual cultivation. The provision of better seeds, the use of manures etc. could be secured by organising what have been called "service co-operatives" for such purposes. In Japan, small farms have achieved a very high degree of agricultural productivity. A co-operative farm may secure some economy by using less labour in different operations. But this is no advantage in a country like India with its large surplus agricultural population, for whom we cannot provide alternative occupations. If the system of co-operative farming is to be introduced on a large-scale, it would involve a considerable amount of compulsion, which may be allright for a totalitarian country, but which is inconsistent with the scheme of things we are proposing to adopt.

Moreover, the Indian experience with the working of co-operative farming has not also been encouraging. Reports on their working so far gave a rather discouraging picture of their operations. These societies were found to have been organised mostly by large landholders who wanted to evade the consequences of land reforms legislation.

Hence it is undesirable to lay so much emphasis on the introduction of the system of co-operative farming. Co-operative farms would tend to be unstable and liable to be broken up by disputes. They cannot be maintained on a permanent basis except on the basis of compulsion. But this is not to deny the utility of such a system. Co-operative farming may be worked successfully if conditions are otherwise satisfactory. But before this is done, intensive propaganda has to be carried on to create the necessary climate for making such a method of cultivation successful.

Another serious limitation is the absence of adequately trained personnel to run the co-operative farms. As the organisation of these farms would be larger, their management would require the services of educated men who have been thoroughly trained in the co-operative principles. In fact, one of the reasons for the slow progress of the co-operative movement in this country is the lack of trained personnel.

In this connection a reference may be made to a proposal by Dr. Otto Schiller, a German expert on agricultural economics. According to him, the advantages of large-scale in farming operations can be obtained by retaining the present system of small holdings. This should be combined with the organisation of a special type of co-operative society for the purpose of undertaking joint planning of production, marketing and other necessary functions. It will then be possible to have both the advantages of joint cultivation and those of individual initiative and attachment to the soil.

Proposed organisation of co-operative farms : One of the charges brought against the movement for co-operative farming was that the government had no clearcut ideas as to how such farms should be organised. The Government of India appointed a Working Group on Co-operative Farming, which issued its report on the last day of 1959. The main recommendations of the Working Group are given below.

The Group recommended that the area of operation of a co-operative farming society need not necessarily cover one entire village so that there may be more than one such society in a village. The Society should be formed purely on a voluntary basis for five years in the first instance. But the members would have the right to withdraw even during these five years. When a member withdraws he should get not necessarily the same plot of land he contributed, but land of equal productivity situated at the periphery without dislocating the scheme. When a member supplies cattle, implements etc., besides land, the value of these resources should be treated either as deposits or share capital. The members shall form the general committee which should approve the various plans relating to production and development etc. The expenditure should be sanctioned by the President, disbursements to be made by the Treasurer and accounts maintained by the Accountant-cum-Secretary to minimise chances of misappropriation of funds. The society should insist that all members should work on the farm and

absentees should not normally be admitted as members. It should evaluate the differences in skill and ability of the workers and attempt should be made to fix "norms" on lines of traditional standards and prevalent practices. Workers should be rewarded on that basis. A substantial part of the net profits should go to the members as bonus for work done, and provision may also be made for meeting ceremonial and unforeseen expenditure by ear-marking 10 p.c. of the net profits to Mutual Aid Funds. The society should not take upon itself the liability for the prior debts of a member. But there should be no ban on the admission of such persons as members. The society should advance loans for ceremonial and other purposes and loans might be given for consumption needs of its members also.

The Group recommended government participation in the share capital of a society in order to strengthen its financial partition. But such contribution to the share capital should not exceed Rs. 2000 per society, and it should be retired over a period of 10 years. The government should also grant the long-term and medium-term loans to the societies, while short-term funds should be advanced by the central financing agency to which a farming society would be affiliated.

The Group also made a number of recommendations for popularising these societies. Advisory Boards should be set up immediately at the State and National levels for planning and promoting co-operative farming. The Report envisages the establishment of 320 carefully planned pilot farms in co-operatively advanced NES blocks and the organisation of 10 societies in each block in the next 4 years. For this purpose a special officer on co-operative farming is to be attached to each block. The demonstration effect of the successful co-operative societies would inspire others and bring about 20,000 new societies by the end of the Third Plan. The government should also set up a National Institute of Co-operative Farming and organised 160 training centres throughout the country in the next 4 years. Promising young farmers and village leaders should be given a two weeks training course and seminars should be conducted in the villages for 3 days to acquaint the members with the operation of these societies.

Thus for the first time we have here a blue-print of the organisation of a co-operative farming society. Many of these features are no doubt admirable. But they are unlikely to meet the objections that have been

raised against the system. It would be difficult to organise such farms on a large scale and to work them successfully in view of the apathy, ignorance and the known quarrelsome attitudes of the villagers.

Questions

1. Discuss the different proposals which have been made to solve the problems of the sub-division and fragmentation of agricultural holdings in India. (C. U. B.Com. 1957 ; Ag. 1954 ; Del. 1953, 1959 ; Bom, 1954 ; Utkal, 1957),

2. Examine the case for and against co-operative farming in India. (Raj. 1958 ; Del. 1958 ; Bom. 1957 ; W. B. C. S. 1957).

3. Write notes on Co-operative Village Management. (Gau. 1952 ; Cal. Hons. 1952).

CHAPTER 9

IRRIGATION

Importance of irrigation : The importance of proper provision or irrigation facilities is quite obvious in an agricultural country like India. Land does not usually yield good crops unless it gets a plentiful supply of water. This is specially true in India where the soil is comparatively dry. Land can be given adequate quantities of water from two sources *viz.*, rainfall and artificial irrigation. Though India belongs to the monsoon area, rainfall is insufficient in many parts of the country. In those areas where it is adequate, difficulties are caused by the uncertainties of the rainfall. There are certain types of crops like rice or sugarcane which need a regular and steady supply of water, hence it has become essential to construct irrigation works in order to lessen our dependence on the monsoons.

Kinds of irrigation works : There are four main sources of irrigation works in India, *viz.*, wells, tube-wells tanks and canals.

Wells : These constitute an important source of supply of water, important because their construction is within the resources of the individual cultivators. This form of irrigation has been highly developed in U.P., Punjab, Madras and Bombay. There are about 1·66 million wells in the country in which about Rs. 100 crores have been invested. These have been constructed mostly by the cultivators to many of whom the government granted takavi loans, temporary exemption from the payment of higher rent etc.

Tube-wells : This source is being utilised only recently and has been developed extensively in U.P. The Ganges Valley Tube-well Irrigation scheme of that state made provision for the construction of 1700 tube-wells, which are pumped by electricity. Since then a large number of tube-wells have also been sunk in U.P., Punjab, Bihar and other states. Wells irrigated about 30 p.c. of the total irrigated area.

Tanks : These are an ancient source of irrigation, and are to be found in almost all states except Punjab. Madras contains the largest number of tanks, *i.e.*, 35,000. While wells are mostly constructed by private persons, tanks are almost always owned by the government. Tanks irrigated about 20 p.c. of the total irrigated land in 1956 57.

Canals : By far the largest part of the irrigated area gets its water-supply from the canals. They are also an ancient source of irrigation, having been constructed both in Hindu and Muslim periods. These canals have been constructed mostly by the state, and irrigated about 50 p.c. of the total irrigated area.

They are of three types, *viz.*, perennial, innundation and storage. The *perennial type of canals* contains a steady supply of water throughout the year. This is done by constructing a barrage across the river in such a way as to maintain the river water at a sufficiently high level so that there is always a steady supply of water in the canals. *Innundation canals* receive water from the river only when it rises above a certain level. Hence these canals contain water only during particular seasons of the year. In the *storage canals*, rain-water is stored up during the monsoons in hunger reservoirs by constructing dams across the mountain valleys. This water is then used to irrigate the surrounding areas in the dry part of the year. This type of canals is to be found mostly in Madras and Madhya Pradesh.

Extent of irrigated area : In undivided India about 24 p.c. of the total acreage was irrigated. After partition, the proportion of irrigated to the cultivated area had fallen to about 17 p.c. By the end of the Second Plan the area brought under irrigation has increased to about 27 p.c. of the total cultivated area.

Classification of irrigation works : Irrigation works are now classified by the government into two groups, *viz.*, productive and unproductive. Productive works are those projects which are expected to yield a net revenue sufficient to cover the interest on the capital invested within a few years. Unproductive works are not expected to yield the required revenue.

Benefits of irrigation : Irrigation works confer very great benefits on the country. In the first place, land, which is irrigated properly, generally yields larger crops than unirrigated land. As the amount of rainfall is uncertain as well as inadequate, the yield from unirrigated land is also uncertain, whereas that from irrigated land is more certain. Thus irrigation is an important means of stabilising agriculture in areas of precarious rainfall. Secondly, considerable part of the land at present lying waste can be brought under cultivation if irrigation facilities are provided. Thirdly, irrigation works, by ensuring

a steady supply of water, provide good protection against the ravages of famine. Lastly, irrigation works yield some revenue to the states in addition to improving agriculture.

Irrigation in the five-year plans : After the achievement of independence in 1947, the Government of India realised the need for constructing more irrigation works in the country in order to increase the production of food crops. A large number of irrigation works were started in different states. These works can be classified into two groups :—multi-purpose projects and other irrigation works. The multi-purpose projects are so called because they are meant to serve many purposes, *viz.*, irrigation, generation of electricity, flood-control etc. Among these projects, mention has already been made of the Damodar Valley Project, the Hirakund Dam Project, Bhakra and Nangal Project etc.

The Five-Year-Plans rightly give emphasis to the need for more irrigation works. The First Plan, therefore, made provisions for the expenditure of Rs. 226 crores on the various multi-purpose and power projects and Rs. 168 crores on the construction of other irrigation works. The aim was to complete the projects which had already been started and it had been estimated that when these projects were completed and fully developed, they would irrigate an additional area of 16·9 million acres of land and generate 1·46 million kwt. of electricity. In addition to those already begun, some new schemes were also started. These were the Koshi Project in Bihar and Nepal, which was expected to irrigate about 2630,000 acres and to generate 40,000 kwts., of electricity and was also to help in flood control ; Rihand Project in U. P., irrigating 35,000 000 acres and generating 240,000 kwts.; Koyna Project in Bombay, irrigating 33,00,000 acres ; Krishna Project in Andhra and Madras and the Chambal Project in Madhya Pradesh and Rajasthan.

The First Plan provided for the execution of nearly 300 large and small projects. By the end of that Plan period, about 30 lakhs acres of land were brought under irrigation by the large and medium-sized projects and another 100 lakh acres by the minor projects. During the Second Plan, an additional area of 100 lakh acres under the minor projects. So by 1961, the total irrigated area increased to 700 lakh acres and this means a rise in the irrigated area by about 62 p.c. during 10 years. The target at the end of the Third Plan was 900 acres.

Major vs. Minor irrigation works : Of late some controversy is going on as to the relative merits of the major and the minor irrigation works. The major irrigation works like the DVC Hirakund dam are no doubt spectacular, and these yield other benefits besides irrigation. These have also created a large irrigation potential. But unfortunately not all of this potential is being used for a numeber of reasons. For example, according to the Deputy Chairman of the Planning Commission, only about 50 p.c. of the irrigation potential created during the First Plan were actually utilised by 1958. The construction of these irrigation projects involved heavy expenditure of money. Would not it have been better, it has been argued, to have spent this money on minor irrigation works like wells, tanks etc., where the proportion of the utilisation of the irrigation potential is very high ? The latter would have involved much less expenditure of money while the yield of crops would have increased by a larger percentage.

There are several reasons for the low utilisation of the large irrigation projects. In the first place, the canal systems have been badly designed in some cases and carried out. The layout and the construction of the distributory canals had not been done after considering the special needs of, each locality and the level of land in different areas. As a result, all the lands that could have received irrigation did not get it. A second difficulty has been that on some projects, the headworks have been completed, but the construction of subsidiary channels, which was the responsibility of the villagers, was not completed.

A third difficulty has arisen on account of the levy of water rates. These irrigation projects have been very expensive as they were carried out during periods of very high prices. So the rates charged for the supply of water from the canals have been rather high, or were regarded as high by the cultivators. In some cases the basis for fixing these rates had also been arbitrary. As a result, cultivators have shown in many areas an extreme unwillingness to use water on payment of such high charges. To overcome this reluctance to use water, rates should be fixed on a more reasonable basis, taking account of the net benefits from irrigation rather than the expenses incurred, and concession should be granted during the first few years.

It has also been found that in certain areas, the newly irrigated areas do not possess adequate fertility and a greater use of fertilisers and manures would have to be made before the full benefits from irrigation could be obtained. In such areas the difficulty can be solved by organising an irrigation extension service for promoting the use of fertilisers and improved farm management practices.

Another major problem of canal irrigation has been water logging of land. This has been due to defective drainage planned and designed without proper surveys. The construction of embankments for flood protection has adversely affected the natural drainage of the areas, and it has also prevented the deposition of fertile soil that the flood waters from the rivers used to leave on the land. Where such embankments are put up, sluice gates at regular intervals should also be constructed for this purpose.

All these factors have led to the partial utilisation of the irrigation facilities constructed at so great a cost. These have to be remedied as soon as possible. One thing should, however, be borne in mind. The utility of these large irrigation projects should not be judged only in terms of their impact on the provision of irrigation facilities alone. These are generally multi-purpose projects, yielding a large number of benefits, whose effect may not at once be visible, but is nevertheless (like flood control) of a very great long-term character. But what has been a most serious defect is the neglect of existing minor irrigation works. The maintenance of these works was previously done by the landholders, and after the abolition of the Zemindari system, the latter were naturally not looking after these works. On the other hand, the government has not evolved an appropriate organisation to carry out these repairs. This defect should be remedied, and certainly more attention should be paid to the minor works than had been done so far.

Questions

1. Describe the various system of irrigation in India, and point out their economic significance. (Ag. 1938 ; Cal. 1937 ; Del. 1932 ; Punj. 1939 ; Pat. 1957)

2. Briefly describe the principal irrigation and hydro-electric works undertaken in India since 1947 and point out their economic conquences. (Punj. 1953, 1958).

3. What do you know of the Damodar Valley Project ? Estimate the effects it will produce on the wealth and welfare of West Bengal. (Del. 1953 ; Cal. 1949).

4. Describe the principal river valley projects in India. Point out their influence on Indian agriculture and industries. (Ag. 1953, '55 ; Punj. 1955, '56 ; Luck. 1954 ; Pat. 1957)

CHAPTER 10 FINANCING OF AGRICULTURE

All undertakings depend upon finance. Agriculture is no exception to this rule. Its need for finance is no less urgent than that of a large-scale industrial unit. The cultivator needs finance to meet his current requirements, such as for buying seeds, manures, feeding staff etc. He must have money to buy land or to carry out necessary improvements to his land like the construction of wells, fences, drainages, reclamation and other long-term purposes. While his necessity is no less urgent, his difficulties are greater than those faced by his industrial brother. His unit of production is usually small, and his income is highly uncertain, being at the finance of the monsoons and the nature. The sources for the supply of finance are also much less organised or adequate than those in the case of the industrialists. The problem is very much complicated in India on account of the existence of large indebtedness among the peasants. Lack of adequate finance is, therefore, one of the most important causes of low agricultural productivity. In this chapter we propose to study the problem of the supply of short-term finance to meet current requirements.

A. Existing agencies of finance : The cultivator, like all business-men, may finance his operations by drawing upon his own resources. But it is well-known that the vast majority of the cultivators do not possess enough resources for this purpose. Hence they have to depend on outside sources for the supply of necessary finance and have to borrow. The total amount of short-term finance required by the cultivators has been variously estimated. In 1951 the Reserve Bank of India estimated the total short-term and medium term capital needed in agriculture to be Rs. 500 crores. This estimate was made on the basis of the fact that in Bombay the average short-term loan issued by the co-operative societies to an agriculturist family was Rs. 100. The Grow More Food Enquiry Committee of 1952 estimated the total annual requirements at Rs. 800 crores, on the assumption that the needs for annual agricultural operation for an acre of wet land was Rs. 60 and of dry land Rs. 20. The principal source from which they may borrow are (1) the money-lenders, (2) the indigenous bankers, (3) co-operative societies, (4) commercial banks and (5) the government.

(1) *Money-lenders* : They are the most important sources of supply of finance to the cultivators. We have unfortunately no statistics

of the total amount of funds supplied by these people. But there is no doubt that they supply the bulk of rural finance. The majority of these money lenders generally combine this business with some form of trading, acting either as merchants or as commission agents. Quite a number of landlords and the large holders acted as money-lenders. Their methods of business are prompt and elastic and they give spot finance. The borrower approaches them direct, and he is not bothered by many formalities. The local knowledge and experience possessed by these money-lenders and their presence on the spot enable them to lend to borrowers who are not always in a position to provide tangible assets.

Unfortunately the finance supplied by the money-lenders has not always been a blessing. In the first place, the ease and facility of borrowing have resulted in improvidence and extravagant habits. Secondly, money-lenders charge very high rates of interest on their loans. It has been found that the rates of interest charged by money-lenders varied between 9 to 36 per cent in Bombay. In M. P., 25 per cent was the usual rate. Part of this high interest rate is, of course, intended to cover the risk of loss as the majority of borrowers are not punctual in repaying loans and cannot afford to furnish good securities. But such high rates have been one of the most important causes of growing indebtedness, and impoverishment of the cultivators. Lastly, quite a large number of money-lenders have been dishonest, and have not hesitated to take recourse to unfair practices to exploit the borrowers. They do not follow any regular system of accounting ; do not give regular receipts for money received and often take bonds for higher amounts then the sums lent. If they are also a merchant or a commission agent, they force the borrowers to sell the produce to them at low prices.

As everybody recognised that in spite of these malpractices, it would not be possible for us to dispense with their services for a long time to come, attempts have been made, especially since 1930, to pass laws for controlling and regulating the activities of the money-lenders.

The following table 20* gives some rough idea of the extent of the operation of the money-lenders.

* Report of the Grow More Food Enquiry Committee, June, 1952. P. 60.

Table 20

State	No. of money-lenders registered or licensed	Amount lent Rs. in crores
Bihar	29 684	15·8
Bombay	25,229	9·44
Madhya Pradesh	9,196	Not available
Punjab	276	"
Hyderabad	15,875	"
Mysore	349	"

In addition, the larger landholders who cultivate their own lands can find from their own resources the short-term finances needed by them.

(2) *Indigenous bankers.* These do not undertake the function of supplying funds directly to the cultivators. Their part is mainly indirect. They finance the movement of crops from the villages to the main marketing centres and the ports. The village money-lenders also borrow funds from them for the purpose of lending to the cultivators.

(3) *Co-operative societies.* The co-operative credit societies have been organised in the 19th century mainly under the auspices of the government. These are formed by the cultivators themselves who organise the society to raise funds and to lend them to members. These primary credit societies sell shares, accept deposits and borrow funds from the central co-operative banks located in district or taluka head-quarters. The money thus obtained is lent to the members to meet their current requirements. In 1960-61, the co-operative societies included 170 lakh members and granted loans, amounting to Rs. 202 crores. It is easy to see that their resources are inadequate to meet the requirements of the cultivators. According to the Report of the Rural Credit Survey about 3·1 p.c. of the financial needs of the cultivators was provided by the co-operative societies.

(4) *Commercial banks.* In India, the commercial banks have not taken part in financing the needs of the cultivators. They provide less than nine per cent of the credit obtained by the cultivators. They have confined their operations mostly to bigger towns and mundis and

do not lend again the security of land, the only security that the cultivators can furnish.

(5) *The Government.* The governments of the States have also taken some part in meeting the financial needs of the cultivators. They grant two types of loans, short term loans granted for the purchase of seeds, manure, cattle etc., under the Agriculturist's Loans Act of 1884, and relatively long-term loans financing permanent improvements in land under the Land Improvement Loans Act of 1883. These loans are called *taccavi* loans. The amount of these loans is very small as compared to the total needs of the cultivators. The government provided 3·3 p.c. of the credit obtained by the cultivators. Moreover, they are generally granted during periods of distress or crop failures. They are, therefore, an emergency source of credit, rather than a regular one on which cultivators may depend. Too many formalities have to be followed in getting those loans, which can be obtained after a good deal of delay. The method of collection is also very rigid. The cultivators have to pay back on the due date, as otherwise distress warrants may be issued against their properties. As a result, these loans have never been popular with the cultivators.

Thus it is obvious that the bulk of rural finance is still now supplied by money-lenders under conditions which operate heavily against the cultivators. Co-operation has touched only the fringe of the problem, and the government comes in only occasionally, specially during periods of distress. This is the over-all picture of the organisation of rural credit in our country. The picture will, however, be incomplete unless one mentions the part played by the Reserve Bank of India in this sphere. The Reserve Bank does not provide finance directly to the cultivators. Its role is mainly indirect. It has been granting increasingly large amount of loans to the co-operative banks. In 1965-66, the Reserve Bank granted loans worth Rs. 167 crores to the State Co-operative Banks at concessional rates.

Reserve Bank of India and rural credit*. When the Reserve Bank of India was established in 1934, it was expected to take part in the provision of rural finance. For that purpose certain provisions were included in the constitution of the Reserve Bank. First, it was

* See The Role of the Reserve Bank of India in the Scheme of Agricultural Credit by V. Sivaraman in the *Reserve Bank of India Bulletin*, April, 1952. P. 269-75.

required to set up an Agricultural Credit Department to study the problem of rural finance and to make suitable recommendations to solve this problem. Secondly, the Reserve Bank was required, under section 17, to grant loans and advances to the co-operative banks through their apex institutions (*i.e.* State Co-operative Banks) for finan ing seasonal agricultural operations or the marketing of crops. The Bank was also to grant loans and advances to the State Co operative Banks against government securities and land-mortgage bank debentures. Lastly, the Reserve Bank was to grant loans or advances to the State Co-operative Banks against their promissory notes, supported by documents of title to goods. The period for which loans are to be granted for seasonal agricultural operations or marketing of crops was 9 months against 3 months in the case of ordinary loans. By another amendment, this period has been extended to 15 months.* In spite of these provisions, the part played by the Reserve Bank in granting loans and advances to the co-operative movement was comparatively small, as would be evident from the fact that in 1946-47, the amount of such loans was only 1·5 lakhs. Since 1942, the Reserve Bank announced that it would grant such loans at one (later raised to one and a half) per cent below the Bank Rate, *i.e.* at 1½ p.c., the Bank Rate remaining at 3 p.c. throughout this period. In other words, while other borrowers from the Reserve Bank had to pay 3 p.c. on their loans, the State Co-operative Banks paid only 1½ p.c. But since 1947, the Reserve Bank has been playing an increasing part in the provisions of rural finance. The amount of loans granted by it to the State Co-operative Banks increased from Rs. 16·8 lakhs in 1947-48 to Rs. 11·3 crores in 1951-52, Rs. 57·0 crores in 1957-58, Rs. 100·65 crores in 1959-60, and Rs. 110 crores in 1960-61 and to Rs. 167 crores in 1965-66. The amount advanced by the Reserve Bank formed about 50 p.c. of the total outstanding of advances made by the primary agricultural credit societies.

This had been made possible as a result of a number of concessions granted by the Reserve Bank. For example, till recently, all accommodation granted by the Reserve Bank to the State Co-operative Banks had to be repaid by a fixed date. This caused a certain amount

* By a recent amendment passed in 1953, the Reserve Bank has been authorised to grant loans for agricultural purposes for periods ranging for more than 15 months but not exceeding 5 years subject to government guarantee of such advances. The total of such advances must not exceed Rs. 5 crores.

of difficulty to the co-operative banks and so the Reserve Bank has decided to allow loans taken by the co-operative banks to run for their full periods. Secondly, the Reserve Bank has continued granting these types of loans at the old rate of one and a half per cent, though the Bank rate was raised from 3 to 3½ p.c. since November, 1951.

These loans are granted to finance short-terms requirements of the co-operative movement. The Reserve Bank is also taking an indirect part in financing the long-term requirements of agriculture. The Bank has begun to subscribe to the debentures of land-mortgage banks which are guaranted by the state governments.

All this is encouraging. It has, however, been urged that this is not enough, and that the Reserve Bank ought to take a larger part in providing finance for agriculture. This desire is no doubt understandable. But the difficulty lies in determining the manner in which the Reserve Bank is to grant more loans to agriculture. As a distinguished writer has pointed out, the central bank can grant more loans to agriculture "only if the latter is organised on a large-scale and is in a position to provide good credit-worthy borrowers ; or where it is not so organised, there should exist proper organisations for marketing and other purposes to which the central bank can extend credit with safety."* This can be done if the co-operative movement is properly strengthened and re-organised so as to embrace the rural population. Suggestions along these lines have been discussed in the next chapter.

Suggestions for reform : In view of the difficulties which cultivators feel for the lack of adequate finance, it has been suggested that the government should take steps for the establishment of an *Agricultural Credit Corporation.* The adoption of such a proposal was made by the Agricultural Finance Sub Committee of the Governmentment of India (the Gadgil Committee). Pakistan has already set up an Agricultural Development Finance Corporation in 1952 for providing financial facilities to agriculture. This Corporation has an authorised share capital of Rs. 5 crores of which Rs. 2 crores have been issued initially. 51 p.c. of the shares has been taken up by central government and the rest were taken up by the state governments, banks and other financial bodies.

* S. N. Sen. *Central Banking in Undeveloped Money Markets.* (3rd Ed.) P. 253

But the desirability of establishing such an institution may be questioned. The corporation, when set up, cannot lend directly to the cultivators, the vast majority of whom are not in a position to furnish adequate securities. It will have to lend through the co-operative banks. But unless it can be shown definitely that the co-operative institutions cannot borrow the necessary amount from the Reserve Bank, there is very little justification for setting up such a central lending institution for agriculture.†

There is no doubt that the only way to solve the problem of rural finance is through the reform of the organisation of the co-operative movement. The whole position has been examined by the Committee on the Survey of Rural Credit set up by the Reserve Bank. That Committee have made a number of valuable suggestions of reorganising the system of rural credit. These will be examined in the next chapter.

B. **The problem of agricultural indebtedness :** Another most unsatisfactory feature in our agricultural organisation is the existence of large indebtedness of the cultivators. That the farmers have always to borrow is not peculiar to India. This is true of every country. But in India the problem has become acute on account of the chronic poverty of the cultivators and the unproductive character of the most of the debts contracted by them.

Various estimates have been made from time to time regarding the extent of agricultural indebtedness in our country. In 1895, Sir F. Nicholson estimated the total rural debts to amount to Rs. 45 crores in Madras. On the basis of the same estimate, Sir E. Maclagan calculated the total rural debts of British India to be Rs. 300 crores. Sir M. L. Darling made the next estimate. According to his calculations, the total agricultural debts in Punjab amounted to 90 crores, averaging Rs. 76 per agriculturists, and the total debts in British India were not less than Rs. 600 crores. The Central Banking Enquiry Committee estimated the total indebtedness to be Rs. 900 crores in 1930 31. The burden of such debts rose heavily in the thirties on account of the fall in agricultural prices and the occurrence of distress in the rural areas. The rise of prices during and after the last war probably gave some relief to the cultivators. But there is no doubt that this relief was not enjoyed by the small cultivators and landless labourers. All

† Such a Corporation has been set up in 1963. See P. 105-6.

evidence shows that at the present moment indebtedness is again on the increase among the cultivators on account of a variety of reasons.

According to the Reserve Bank's Rural Credit Follow-up Survey 1956-57, the outstanding debt amounted to about 10 p.c. of the value of the owned land and 6 p.c. of the value of their recorded assets.

Causes of indebtedness : It is not difficult to find out why cultivators have to borrow and are unable to repay the loans. The vast majority of the cultivators are proverbially poor. They have usually very small incomes which are often uncertain. The holdings they cultivate are small in size, and are getting smaller with each passing generation. Small holdings mean small amount of crops and low income. The decay of the village industries has deprived them of the alternative or supplementary sources of income. Hence their incomes remain low. They are, therefore, not in a position to save anything, and no wonder that they have to borrow on every occasion.

Such occasions also arise frequently. If the rains fail or if there is too much rain there will be crop failure and the cultivator must then borrow to pay rent and to maintain his family. Or if the cattle dies, he has to borrow to replace his live-stock. The demand for the payment of rent by a fixed date may also force the cultivators to borrow for paying the land revenue.

Another prominent factor causing indebtedness is the improvident habits of the majority of the cultivators. They are too fond of litigation and did not hesitate to borrow money for the conduct of a useless suit or for redressing some fancied grievance. The cultivators have also been forced by the conventions of their society to spend beyond their means to perform the *Sradh* ceremonies of their parents, or to marry their daughters. According to the Rural Credit Follow-up Survey Report, about 40 p.c. of the debts were incurred to meet family expenditure.

The malpractices of the money-lenders are also an important cause of agricultural indebtedness. Money-lenders charged very high interest rates and often cheated the illiterate, helpless borrowers by falsifying the accounts. The burden of debts increased heavily as a result of these malpractices.

Lastly, in the pre-British days there was some check on the activities of the money-lenders. The village community looked after the

interests of the borrowers. Further, on account of the rule of *Damdaput* money-lenders could not demand more than double the original sum they lent. This put an automatic check on the growth of debts. Lastly, it was then not so easy to sell land and the money-lender had therefore to depend on the goodwill of the borrowers for getting his money back. But during the British rule with the disintegration of the village communities, the rule of *Damdaput* became a dead letter and the burden of debts amounted higher and higher. The civil law favoured money-lenders who could bring suits for the recovery of loans and could attach the lands of the borrowers in case of a failure to repay loans.

Effects of indebtedness : The results of such heavy indebtedness have been extremely undesirable. Once in debt, always in debt. The cultivators, who often borrowed injudiciously for unproductive purposes, soon found themselves dispossessed of their land. As a result, the number of landless labourers increased, giving rise to discontent. In many cases, money-lenders, after buying the land, settled it with the borrowers who become tenants, paying higher rent. They lost all incentive to improve cultivation. The result was a loss in productive efficiency. As many money-lenders also combined their business with some trading operations, they often forced the borrowers to mortage their standing crops to them. These crops, when harvested, had to be sold to the money-lenders at prices dictated or fixed by the latter. So the cultivators could not get proper prices even for the small amount of crops grown on their tiny plots of land. There is no doubt that such heavy indebtedness stands in the way of agricultural improvement.

Measures for relief : The problem attracted the attention of the government in the latter part of the 19th century. Since then, a number of measures have been adopted to bring relief to the cultivators. In the first place, the government sought to amend the law in order to prevent some malpractices. For example, the Deccan Agriculturist's Relief Act of 1879 allowed the civil courts to reduce the rates of interest. Creditors were obliged to furnish written accounts and to give proper receipts for all repayment.

Secondly, it was sought to place restrictions on the right to transfer land in order to prevent borrowers from mortgaging their land. The *Punjab Land Alienation Act* of 1901 laid it down that land held by an agriculturist could not be sold to a non-agriculturist, nor could it be

mortgaged for more than 20 years. The Act was copied in some other states. The object of this Act was to prevent the passing of land from cultivators to the money-lenders. The utility of the Act had been called in question by a larger number of writers. According to them, it had not prevented the passage of land from borrowers to money-lenders as the more prosperous agriculturists adopted the profession of money-lending and the provisions of the Act did not apply to them. The Act, moreover, resulted in a restriction of credit. These Acts have been repealed under the new constitution.

Thirdly, the government also tried to provide cheap credit to the cultivators. This was sought to be done in two ways. First, the government passed two Acts,-the Land Improvement Loans Act of 1883 and the Agriculturist's Loans Act of 1884. Under the former Act, it granted loans to cultivators, repayable over long periods, in order to enable them to carry out permanent improvements to land. Under the second Act, short term loans were granted for current agricultural needs. These loans are called *Taccavi* loans. These loans are given mostly during periods of scarcity. They are not very popular with the cultivators as the latter have to go through too many formalities before being granted loans.

The next step taken by the government was to organise the co-operative movement. Acts were passed in 1904 and 1912, under which co-operative credit societies were started. These societies were formed by the cultivators and granted loans to the members. Land-mortgage banks have also been started to grant long term loans for the repayment of debts. But these societies and banks are still too few as compared to the needs of the cultivators.

Debt legislation : All these measures were adopted before the first world war. But while they gave some relief to the harassed cultivators, they failed to solve the problem. The burden of debts continued rising, and matters came to a head with the advent of the world trade depression of the thirties. This depression caused a serious fall in agricultural prices as a result of which the burden of debts grew heavily. The different state governments were forced to adopt a series of measures to cope with the problem of indebtedness. These measures can be divided into two classes, *viz.*, scaling down debts and reform of money-lending. We propose to discuss them one by one.

Scaling down debts : Almost all the States including the previous Native States passed suitable legislation for the conciliation and reduction of debts. Most of these Acts were passed during the years 1933 to 1939. Conciliation of debts was first carried out in Madhya Pradesh in 1933. Under this methods, the government established a large number of Debt Conciliation or Debt Settlement Boards in different areas of the State. These Boards heard petitions submitted by borrowers and served a notice to the creditors requiring them to submit detailed accounts of debts owned by borrowers. They then tried to induce creditors to agree to accept, in settlement of their loans, sums within the paying capacity of debtors. They might also fix instalments ranging over a period of 15 to 20 years for the repayment of debts.

At first, these settlements were made on a voluntary basis. But soon it was found necessary to introduce a measure of compulsion. In some Acts, it was, therefore, laid down that if creditors to whom 10 p.c. of the debts of a borrower (in Madras 50 p.c.) were owed and agreed to accept a settlement proposed by the Board, it was to be decreed as binding upon other creditors. If some of them refused to accept the settlement, they were placed under certain restrictions. For example, they would not be paid costs of a suit brought for the recovery of the debts ; they would not be paid interest at more than 6 p.c. and their loans were to be repaid only after the claims of the creditors who agreed to the settlement were met in full. In Madhya Pradesh, Debt Relief Courts were granted authority to reduce the principal of debts in proportion to the estimated fall in the value of land. The Madras Agriculturist's Relief Act of 1938 laid it down that all arrears of interest outstanding on Oct., 1937 were to be wiped out, and only the principal was to be repaid. In future, interest could be charged at the maximum rate of 6¼ p.c., and the total liability was not to exceed double the amount borrowed.

In addition to scaling down debts, some of these Acts included provisions for rural bankruptcy. If it was found that the assets of a borrower were insufficient to repay the debts, he would be declared an insolvent, and his assets excluding the homestead land and a certain amount of land for the subsistence of his family were to be sold and the proceeds would then be utilised to repay the debts. These provisions existed in West Bengal, Punjab and Madhya Pradesh.

Regulation of money-lending : Regulation of money-lending has also been an integral part of recent debt legislation. But legislation to curb the malpractices of money-lenders was passed as early as 1879 when the Deccan Agriculturist's Relief Act authorised the courts to examine the account of a debt transaction and to reduce the rate of interest. The next important legislation on the subject was the Usurious Loans Act, adopted in 1918. It authorised the courts to re-open a debt transaction and to reduce excessive rates of interest. But these Acts remained, more or less, a dead letter on account of the illiteracy, ignorance and helplessness of the cultivators. In the nineteen thirties, the government of Punjab took the first step to undertake legislation on this subject by passing the Regulation of Accounts Act in 1930. This was followed by other States.

The main provisions of these Acts related to the registration and issue of licence to money-lenders, regulation of their accounts and limitation of interest rates. Uusually money-lenders had to register themselves and to take out a licence from the government before they were allowed to conduct their business. The licence might be cancelled for non-compliance with the provisions of the Act and for dishonesty. Secondly, every money-lender had to maintain regular accounts of all his transactions, to give proper receipts to all debtors for any repayment and would have to furnish to his debtors a periodic statement of their liabilities. Thirdly, these Acts sought to lay down maximum rates of interest that might be charged by money-lenders. A distinction was made between secured and unsecured loans, the maximum permissible rates of interest being higher on the latter type of loans. These rates usually varied between 6 to 12 p.c. (18 p.c. in M.P.). Lastly, these Acts provided protection to debtors from intimidation and molestation by money-lenders.

A review of the working of debt legislation*: Recent debt legislation has sought to attack the problem of agricultural indebtedness from two directions. It provides for scaling down the amount of debts so as to bring them within the paying capacity of debtors. It has next tried to cure money-lending business of its abuses so that the burden of debts may not grow heavy in the future. What has been the effects of these acts on the organisation and provision of rural finance ?

* For a summary of legislation, see *Agricultural Legislation in India.* Vol. I.

There is no doubt that they have provided some relief to the cultivators. Statistics published in the different States show that a considerable amount of debts has been scaled down. But the amount actually scaled down forms only a small percentage of the total estimated debts. The problems, therefore, remains to be solved. Moreover, certain defects have been found in the working of the Debt Settlement Boards. On account of their illiteracy, debtors have failed to furnish the names of all creditors. Members of some Boards have been found to be corrupt and inefficient. These defects are of course remediable. But a most serious defect has been the absence of any provision for the regular repayment of the scaled-down debts. Debtors were left to repay the instalments out of their own resources. As these proved insufficient, many of them defaulted in their payments. There was no doubt that if creditors knew that they would get back their money quickly if they agreed to settle, many of them would probably have agreed to accept smaller sums in settlement of their claims. But there was no such machinery to ensure speedy repayment. This was a serious defect in the working of the debt settlement legislation.

Efforts to control money-lenders have not, on the whole, proved successful. Strict enforcement of the Regulation of Money-lenders Acts was not possible as that would require a very large administrative machinery. Moreover, as most of the borrowers are extremely needy, they have often been forced by money-lenders to adopt collusive practices to evade the provisions of the law. For example, needy borrowers have to put down in the documents larger sums than they actually borrowed in order to compensate the money-lenders for the low rates of interest they are forced to charge by law.

One result of the working of both these types of legislation has been the restriction of credit facilities in the villages. Cultivators are now finding it increasingly difficult to get new loans. Money lenders are unwilling to lend except to old and trusted borrowers who agree not to go to the courts and to adopt collusive practices. They are also unwilling to lend to debtors whose debts have been scaled down by the Boards until the last instalment has been paid. Opinion is, however, divided on the question whether such a restriction of credit is harmful or not. It has been argued that such a restriction of credit is, on the whole, beneficial as it would discourage borrowing for unproductive purposes.

These laws have provided palliatives. But they have not solved the problem of rural indebtedness. As one writer has aptly put it, these laws are of "the nature of ambulance work, stopping bleeding and the source of further infiltration of the disease, by applying antiseptics and bandaging". They do not go to the root of the problem. Unless proper remedies are found for the causes that force cultivators to borrow, a lasting solution of the problem cannot be expected. While it is desirable that the malpractices of money-lenders should be curbed, it is necessary to remember that their services are indispensable in the prevailing state of credit in rural areas. Effective measures should, therefore, be taken to harness the experience and knowledge of the money-lenders to the organisation of rural credit. The crux of the problem is extremely low incomes of the cultivators. A real solution of the problem of rural debts will, therefore, be found only when far-reaching improvements are carried out in agriculture, with a view to raising the incomes of the cultivators.

Questions

1. Describe the arrangements for providing credit to the cultivators. Are they adequate and efficient ? Suggest some improvements. (All. 1937 ; Cal. 1942 ; Del. 1936).

2. What are your suggestions for the re-organisation of rural credit in this country ? (Bom. 1953).

3. Discuss the causes of rural indebtedness in India. What steps have been taken by the government to solve this problem ? (All. 1943 ; Del. 1939 ; Cal. 1950 ; Punj. 1935 ; I.A.S. 1956).

4. To what extent has the debt legislation recently enacted in different States helped to solve the problem of agricultural debts ? (Cal. 1941 ; Punj. 1941).

5. Discuss the role played by the Reserve Bank of India in the provision of rural credit.

CHAPTER 11 AGRICULTURAL FINANCE: LONG-TERM CAPITAL

In the previous chapter we discussed the organisation for providing short-term finance to the cultivators. The peasants also require finance for longer periods as well. They must have money to buy cattle and ordinary farming implements, and loans taken for these purposes can be repaid, not at the end of the agricultural season, but during a much longer period varying from one to five years. This is known as *intermediate-term credit.* They also require loans for longer periods varying from 5 to (say) 25 years for purposes like the purchase of costly implements, or of land or making permanent improvements to land, such as the construction of wells etc.

Need for land-mortgage banks: The organisation for the supply of finance for long periods is also extremely defective. Co-operative credit societies cannot afford to grant such types of loans. Their resources are limited and they cannot afford to lock them up in long-term loans. The money-lenders who provide the bulk of short-term loans do not also like to lock up their money in long-term loans. They prefer the quick and the surer returns of short-term loans. The government, of course, grants some loans for long periods under the Land Improvement Loans Act of 1883. But the funds provided by the government are extremely inadequate, and borrowers do not like the endless formalities involved in the granting of government loans. There is, therefore, a great need for setting up institutions for supply of long-term finance to agriculturists.

General features of land-mortgage banks*: The experience of other countries shows that long-term loans to agriculturists are best provided through land-mortgage banks or land credit institutions. Land-mortgage banks have been organised either on the co-operative principle or on the joint-stock company principle. They obtain their funds primarily by the sale of long-term debentures in the market. These debentures are secured by mortgages on land obtained from the

* See *Land-Mortgage Banks.* (Reserve Bank of India.) 1951.

borrowers. In many cases, governments have guaranteed to repay the principal and interest on these debentures in case the land-mortgage banks fail to meet their obligations. The funds thus obtained are lent to farmers against the mortgage of their land are generally repayable in small annual instalments over a number of years.

Land-mortgage banks in India : The earliest attempt at establishing a separate land-mortgage bank was made at Jhang in Punjab in 1920. Madras followed suit by organising two land-mortgage banks in 1925, and Bombay by establishing three banks in 1929. The movement then spread to other States.

Madras holds the pride of place in the organisation of land-mortgage banks. Though the first banks were started in that State in 1925, the real beginning came after the establishment of a Central Land-mortgage Bank in 1929 for centralising the issue of debentures. In the course of the next 20 years the number of primary banks have increased to 119 in Madras. Bombay organised the Provincial Land-mortgage Bank in 1935, and high hopes were entertained about the progress of land-mortgage banking in the State. But the progress achieved has not been as satisfactory as in Madras. In 1960-61, there were 18 Central Land-mortgage Banks in Madras, Bombay, Mysore, Andhra and other States. The number of primary land-mortgage banks in all States amounted to 463 at the end of 1960 61. In 1960-61, they advanced loans amounting to Rs. 717 lakhs. The movement has, however, made insignificant progress in the States of West Bengal, Assam, U.P., Rajasthan etc.

Most of the Central Land Mortgage Banks are organised on a quasi-co-operative basis. They have been formed by the primary land-mortgage banks and individual shareholders. Their primary business is to float debentures, and to co-ordinate the working of primary banks. They advance loans mainly for repayment of past debts, for the purchase and improvement of land. Loans are given up to one-half of the value of the land mortgaged and the period of the loan is 20 years, repayable in equal annual instalments. The land-mortgage banks receive assistance from the government in various ways. In Madras, for example, the government has guaranteed the payment of interest and the repayment of debentures issued by the

Central Land-Mortgage Bank. The banks have been granted the power to receive defaulted loans by distraint and sale of produce as well as by the sale of mortgaged land without going through the law courts. The operations of these banks are regularly guided and supervised by the Co-operative Department.

In spite of the high utility of land-mortgage banking in India, its development has not made much headway except in Madras, Bombay and Mysore. Even in these States, the bulk of the loans granted by them have been granted for redemption of old debts. This is unfortunate as land-mortgage banks should play greater attention to finance land improvements designed to increase food production. Both in Madras and Bombay, the State governments are trying to encourage these banks to finance land improvements designed to increase food production. Both in Madras and Bombay, the State governments are trying to encourage these banks to finance land improvement. In Bombay, the government have permitted land-mortgage banks to extend loans for the construction of wells, for housing and for the purchase of costly agricultural implements. These loans are to be given at concessional rates, the government undertaking to make up any loss sustained by the banks on that account. It should, however, be remembered that the task of financing of land improvement by land-mortgage banks bristled with difficulties. The banks have no machinery to examine and assess the various schemes of land improvement.

Land-mortgage banks have gained a new significance on account of the urgent need for increasing food production. Where such banks have worked well as in Madras, they have not only saved many farmers from losing their land during the years of depression, but have also succeeded in reducing their burden of debts. What is now necessary is that these banks should now turn to an increasing extent to the task of financing the long-term requirements of the farmers for carrying out various schemes of land improvement.

An Agricultural Re-Finance Corporation has recently been set up to provide financial aid to central land-mortgage banks. State co-operative banks, other co-operative societies and scheduled banks to enable the latter to take up the task of financing land improvement projects. (See p. 108-09 for details).

Questions

1. Disscuss the need of the cultivators for long-term credit. Point out in this connection the scope and functions of Land-mortgage Banks. (Ag. 1939 ; Cal. 1943 ; Punj. 1939 ; Mad. 1937).

2. Give a critical account of land-mortgage banks in India and indicate the sources from which they derive their funds. (Cal. 1953).

CHAPTER 12 RE-ORGANISATION OF RURAL CREDIT

The Report of the All-India Rural Credit Survey set up by the Reserve Bank of India is a very important document. It contains probably the best discussion of the existing state of rural financial organisation, and has made a number of bold suggestions for devising an "integrated scheme of rural credit."

The report has suggested three-fold organisation for improving the supply of rural credit ; first, a great drive to establish co-operative societies of different types ; second, institutions, both at the National and State levels, for organising a chain of warehouses for the storage, warehousing and distribution of crops ; and lastly, the settling up of a State Bank of India amalgamating the Imperial Bank of India and a number of other State Banks, organised by the former Native States. At each of these stages it has recommended a much greater participation by the State and the Reserve Bank than was the case formerly.

Record of existing credit agencies : Surveys conducted in a large number of places by the Reserve Bank give the following indication of the extent to which the main agencies of rural credit contribute to the total borrowings of the cultivators.

Table 21

Credit agency	Proportion in the borrowings (per cent)
Agricultural money-lenders	24·9
Professional money-lenders	69·7
Relatives	14·2
Traders and Commission Agents	5·5
Co-operatives	3·1
Governments	3·3
Landlords	1·5
Commercial Banks	0·9
Others	1·8

The part played by the co-operatives is thus insignificant, providing a little more than 3 per cent of the total borrowings of the cultivators.

In some States the percentage is still worse. "There are large parts of the country which co-operation has not yet covered. Even in those areas to which it has extended, there are large sections of the agricultural population which still remain outside its membership ; and even in respect of those who are members of co-operative credit societies, the large bulk of the credit requirements is met from sources other than co-operative." Commercial banks and the Government play an almost utterly negligible part in supplying finance to agriculture. Thus for about 94 per cent of their credit requirements the cultivators have to depend on private agencies, the money-lenders and the traders supplying between themselves more than 70 per cent of the total. "The money-lender takes no account of purpose, and charges as high a rate of interest as he can. The trader lends on advances for production, but pays as low a price as he can." Thus the Committee found that rural credit "falls short of the right quantity, is not of the right type and by the criterion of need often fails to go to the right people."

What about the future ? The Committee stated that a proper organisation for rual credit must meet the "long, medium as well as short-term needs ; it must be supervised ; it must be available to all who are credit-worthy and at a moderate rate of interest." There is no escape from the conclusion that it must be organised through some co-operative form if it is to reach down to the enormous number of small cultivators. Co-operation has no doubt failed. But it must be made successful, and hence the Committee concluded that the foremost objective should be to create proper conditions in which co-operative credit might prove successful.

The integrated scheme of organisation : The Committee has, therefore, recommended a concerted drive by each State Government for the re-organisation and spread of the co-operative movement. A definite plan to that effect is to be drawn up by each State Government in consultation with the Reserve Bank. The essence of the re-organisation should be the participation of the Government both in respect of share capital and management. The State Government is to hold a major portion of the share capital of these societies at the apex, district and primary levels. Trained personnel for the keyposts of these co-operative credit societies should be supplied by the State, and for this purpose State Governments should start State Co-operative Administrative and Technical Services. In order to enable the State Governments to

participate in the share capital of the societies, long-term loans should be granted to them out of the National Co-operative Development Fund administered by the National Co-operative Development and Warehousing Board to be set up with funds supplied by the Ministry of Food and Agriculture of the Government of India. These societies should grant short-term credit on the basis of the system of "crop loans". Medium-term loans should also be provided by them. Long-term loans are to be granted by land-mortgage banks to be established in all States. While remaining separate, these land-mortgage banks and co-operative banks should have a common administrative staff, and if possible, a common Board of Directors.

Steps would also be taken to organise co-operative societies for marketing, processing, dairying etc., the State holding the majority of shares as in the case of credit societies. An All-India Warehousing Corporation and State Warehousing Companies should also be set up to build up storage and warehousing centres at important places. The All-India Corporation is to be organised by the National Co-operative Development and Warehousing Board and the State Warehousing Companies jointly by the All-India Warehousing Corporation and the State Governments. These godowns and warehouses should be used not only for the storage of the produce pending its sale, but also for the distribution of such essential commodities as fertilisers, good seeds, and other articles of basic use to the cultivators like kerosene, sugar, matches etc.

Over all these organisations there will be the State Bank of India, a state-sponsored, state-partnered commercial banking institution with an extensive machinery of branches spread over the whole country. This Bank is to be set up by amalgamating the Imperial Bank of India and other State-associated banks such as the State Bank of Saurashtra, Bank of Jaipur, Bank of Patiala, Bank of Baroda, Bank of Mysore, the Hyderabad State Bank etc. The Central Government and the Reserve Bank should hold 52 per cent of the share capital of this Bank, and they should also appoint the majority of Directors. This Bank would pursue a large and expeditious programme of branch banking. It should provide vastly extended remittance facilities for co-operative and other banks, and generally follow a policy of granting advances for agricultural

purposes. It would be responsive to the needs of co-operative institutions for credit, marketing and processing.

The Committee also discussed the part which the Reserve Bank should play in this organisational set-up. The Reserve Bank is to be consulted by each State Government at the time of drawing up of the plans for the development of the co-operative societies. It is to institute a separate Fund to be called The National Agricultural Credit (Long-term Operation) Fund, to which a sum of Rs. 5 crores is to be allotted annually with an initial non-recurring contribution of Rs. 5 crores. Through this fund the Reserve Bank is to grant long-term loans to the State Governments to enable the latter to participate in the share capital of the co-operative societies. The Reserve Bank is also to grant short-term and medium-term loans to the State Co-operative Banks as usual, and the present limit of Rs. 5 crores should be removed. The Reserve Bank should also grant long-term loans to the land-mortgage banks, if necessary, by drawing upon the National Agricultural Credit (Long-term operations) Fund. The Reserve Bank is also to institute another Fund to be called the National Agricultural (Stabilisation) Fund to which Rs. 1 crore are to be allotted annually. This Fund is to be utilised for granting medium-term loans to State Co-operative Banks etc., in circumstances in which the Reserve Bank is satisfied that any of its short-term loans to the latter should not be realised on account of famine, draught, etc. Each State Co-operative and Central Co-operative banks should also set up similar funds, the Agricultural Credit (Stabilisation) Fund, to be used for the same purposes in relation to the loans granted by them to other societies.

The Ministry of Food and Agriculture is also to set up a National Co-operative Development and Warehousing Board with two Funds, the National Co-operative Development Fund and the National Warehousing Development Fund, whose functions have already been pointed out. These Funds would be fed by annual contributions of Rs. 5 crores to be made by the Ministry, besides an initial non-recovering contribution of Rs. 5 crores to the Warehousing Fund.

The State Governments are also to set up State Co-operative Development Funds and State Agriculture Credit (Relief and Guarantee) Fund. The State Bank of India should set up the Integration and Development Fund with money provided by itself, the Reserve Bank

and the Central Government to underwrite any losses incurred in the opening of new branches.

In addition, the Committee made a large number of recommendations relating to the necessity of stabilisation of agricultural prices, proper debt and tenancy legislation, rural savings, finance for rural industries and the development of facilities for the training of personnel.

Implementation of these schemes : Steps have been taken to implement the principal recommendations of this Report. The Imperial Bank of India has been nationalised and re-named as the State Bank of India with a view to foster banking in the rural areas. The Reserve Bank of India have instituted two funds, the National Agricultural Credit (Long-term Operation) Fund and the National Agricultural Credit (Stabilisation) Fund. The first was constituted in February, 1956 with an initial sum of Rs. 10 crores, and the second in June, 1956 with a contribution of Rs. 1 crore. The government has also passed the Agricultural produce (Development and Warehousing) Corporations Act in 1956 for facilitating the formation of Warehousing Corporations throughout the country. Arrangements have also been made to re-organise the co-operative movement in accordance with the recommendations of the Committee.

Comments : This is no doubt a very bold attempt. Its principal merit lies in the fact that it has sought to draw up an integration plan, linking credit with marketing. By combining the warehousing and marketing of crops along with that of the grant of credit, it avoids the serious pitfalls that hampered the smooth functioning of all previous attempts at the re-organisation of rural credit. The move to unite the grant of short-term, medium-term and long-term credit in one comprehensive plan is certainly a step in the right direction. Too often we have suffered from piecemeal attempts to tackle only one problem at a time. These are certainly good features of this integrated plan of development of the machinery of rural credit.

As on former occasions, the main instrument for the grant of credit to the small cultivators is to be co-operative societies, and this after pages of denunciation of the co-operative movement so far developed in the country. This naturally looks a bit queer. The committee pinned its faith on a thorough re-organisation of the co-operative societies. Such a re-organisation is to be carried out through an injection

of state aid,—through an increasing participation of the state in the share-capital and management of the societies. Gone are the days when it was thought that the main reason for the lethargic character of the co-operative movement was its reliance on state aid and guidance ! Time alone will show how the co-operative societies function under increasing state patronage.

Much will also depend on the extent to which the State Bank of India will spread out into rural areas and become one of the principal channels for the supply of credit to the cultivators. To convert a predominantly commercial bank with its whole outlook tinged by the profit motive into a sort of missionary institution charged with the task of taking the Ganges of credit into the far corners of the rural districts is a task which few men could hope to discharge efficiently. The Bank would have to make loans on terms which would not be acceptable to a bank. At the same time it would have to walk wearily, to avoid incurring bad debts in large amount. This is indeed an extremely difficult task, and is bound to involve a good deal of tight-rope walking on the part of the Bank.

Operation of the integrated scheme of rural credit : The scheme of integrated rural credit was based primarily on a re-organisation of the co-operative credit societies. This reorganisation had two features,—*viz.*, formation of large-sized societies, and secondly, State participation in the share capital of these societies. In pursuance of these proposals, steps were taken to set up a number of large-sized co-operative societies, and by 1957-58, about 4470 such societies were brought into existence. Each of these large societies covered on average about 11 villages and their average membership was 418 as against only 64 in the case of the ordinary village societies. The Second Plan target for large societies was 10,400.

But in the meantime serious misgivings were expressed regarding both these features of re-organisation. It was felt that the formation of large societies and increased state participation ran counter to the basic principle of co-operation. The members of such a large society covering several villages would not possess that intimate knowledge of one another that was essential to the success of a co-operative society. State participation would mean the domination of the societies by government servants, which was an undesirable feature. An old co-operator, Sir Malcolm Darling visited India at this time, and submitted

a report which was highly critical of these two features. Within 4 to 5 years, the Government opinion underwent some change and the National Development Council decided in April, 1959 to have two types of societies—small and large one, instead of only large societies. In other words, emphasis shifted again to the small one-village societies. Reserve Bank tried in its Rural Credit Follow-up Survey Report of 1956-57 to point out that "generally speaking, a single village unlimited liability type society found it difficult to organise itself into business concern and to run according to rules and procedures, mainly because of party factions commonly associated with village politics in the context of prevailing socio-economic conditions, and its own inability to employ a full-time trained Secretary". It expressed its opinion that the evidence collected appeared to indicate the superiority of the multi-village societies. But the fashions have already changed and though large sized societies were not disbanded, fresh attempts were no longer made to push on with such type of societies.

The re-constitution of the Imperial Bank of India into the State Bank had already been completed and by the end of June, 1960 that Bank had fulfilled its obligation of opening 400 new branches as stipulated in the State Bank of India Act. The State Bank has also extended its business with the co-operative societies and by the end of March 1959, the total advances granted by it to the co-operative movement amounted to Rs. 12 crores, which was, however, only an insignificant part of its total resources (about 2 p.c.).

Agricultural Re-Finance Corporation : Our previous survey has shown that while something has been done in the sphere of short-term and medium-term credit to agriculture, there is virtually no organisation for meeting the long-term credit needs of the agriculturists except the land-mortgage banks. The Standing Advisory Committee on Agricultural Credit and the Land-mortgage Banks have urged the authorities to set up a central institution to meet this gap. Recently, the government has set up a new organisation for this purpose. An Act was passed in 1963 and the Agricultural Re-Finance Corporation has been established on July 1, 1963.

The authorised capital of the Corporation is Rs. 25 crores, divided into 25,000 shares of Rs. 10,000 each, of which only 5,000 shares have

been issued. The Reserve Bank of India has bought 2500 shares; the State Co-operative Banks and the Central Land Mortgage Banks would take up 1500 shares, and the rest by the LIC, the scheduled banks and other insurance and investment companies. The shares have been guaranteed by the central government both in respect of the repayment of the principal and the payment of a minimum annual dividend of $4\frac{1}{2}$ p.c. In addition, the central government have provided an interest free loan of Rs. 5 crores to be repaid from the end of 15 years. The Corporation may also accept long-term deposits and sell bonds or debentures in the market. The Corporation is to be managed by a Board of Directors consisting of 9 persons, and the Deputy Governor of the Reserve Bank of India in charge of agricultural credit is to be its Chairman.

The Corporation is to act more or less as a central banking institution in relation to the agencies like the land-mortgage banks, which are financing the long-term credit needs of the cultivators. It will concern itself with major projects of agricultural development which cannot be financed either by the central land-mortgage banks or the State Co-operative Banks out of their own resources. The Corporation may grant loans and advances by way of refinance or otherwise to the central land mortgage banks, State Co-operative Bank or other co-operative societies approved by the Reserve Bank of India, and scheduled banks, and to subscribe to the debentures issued by these institutions. These loans and debentures are to be repaid within a period not exceeding 25 years, and these should also be guaranteed by the government. The Corporation will work in close collaboration with the Reserve Bank of India. In addition to schemes of land improvement, the Corporation is also authorised to guarantee deferred payments in connection with the purchase of capital goods from outside by the above-mentioned institutions.

The Corporation is to occupy the same position in relation to long-term financing of agriculture as is being done by the Reserve Bank of India with respect to short and medium-term credit. Its functions are to aid more in financing and strengthening all other institutions engaged in this task rather than being itself a major primary lender.

Questions

1. What are your suggestions for the re organisation of rural credit in India? (C. U. 1956).

2. Appraise the findings of the Rural Credit Survey in India. What measures have been taken to implement the recommendations? (I.A.S. 1956).

3. Write a short note on the organisation and functions of the Agricultural Re-Finance Corporation.

CHAPTER 13 AGRICULTURAL MARKETING

In ancient times agriculture was carried on in India on subsistence basis. The farmers raised sufficient crops to maintain their families, and sold only a small portion of the crops in the market. The problem of marketing was thus comparatively simple. But the character of agriculture has undergone considerable change in recent years. Cash crops like jute, cotton, sugarcane, tobacco etc., are grown largely for sale in the market and a considerable part of the food crops is also offered for sale in the market. The need for a good marketing organisation has, therefore, grown. A good marketing organisation will enable the cultivators to receive proper price for produce.

Defects in marketing : Unfortunately the Indian cultivator markets his produce under the most disadvantageous conditions. If he wants to sell his crops in the open market, he has to face a great many difficulties. He may bring his produce to the village *hats* or markets on the weekly market days. But this is often inconvenient on account of bad roads and transport conditions. Villages do not possess good roads and means of transport are often primitive. Moreover, he cannot always spare the time to attend the market and sell the produce directly. No wonder that the cultivator prefers to sell his crops in the villages to a *bepari* or middlemen.

More often than not, the cultivator is not free to sell his crops in the market. On account of his poverty and other reasons, he has previously taken loans from the village mahajans to whom he is under obligation to sell the crops. These mahajans do not always pay the proper market price to their debtors.

Even if he manages to take his crops to the *mandi* or big markets, he has to face many handicaps. He does not always know the prevailing market price for the variety of crops he has to sell. On account of his ignorance it is inevitable that he should come off second best in his contest with the high specialised knowledge and the vastly superior resources of the buyers. Secondly, as weights, scales and measures are not standardised and regularly inspected, these are often manipulated against the cultivators. Thirdly, he is often forced to pay a large number of market charges on various pretexts. Deductions are made from the price to be paid to him on account of charity, possible loss of weight,

impurities in the produce etc. These deductions often amount to considerable sums.

Fourthly, some of the market practices are reprehensible. The price is often settled under cover. "Both the *arthiyas* put their land under a piece of cloth and start catching one another's fingers. The negotiations go on in this secret manner." The seller does not usually get the proper price as a consequence.

Fifthly, the greatest defect is the fact that there is a whole host of middlemen between the grower and the ultimate consumer, the *beparis, farias, kachha arthiyas, pacca arthiyas* and others. The larger the number of middlemen, the smaller must be the share of the cultivators. These middlemen not only fleece the growers, they also resort to adulteration, dumping and other illegitimate practices. Stone chips are mixed in rice; groundnut and tamarind are soaked in water to increase their weight. As a result of such adulteration and other malpractices, the quality of the produce is lowered. Low quality and reputation inevitably lead to lower prices.

Lastly, another difficulty is due to the fact that most of the cultivators have very little holding power on account of their poverty. They are poor and often heavily in debt. So they are forced to sell their crops almost immediately after the harvest to meet the pressing demand of the money-lenders for repayment and of the rent collectors. Prices generally touch the bottom immediately after the harvest when every cultivator is eager to sell. Thus farmers who have to sell at a most unfavourable period receive the lowest prices.

Thus the high cost and inconvenience of transport, their ignorance regarding market conditions, the unregulated practice of bidding, unreliable weights and scales, the manifold deductions made in the markets, large numbers of middlemen and their malpractices, and the lack of holding power on account of poverty and indebtedness—these are the most important defects in the marketing organisation. As a consequence of these defects, there is a considerable price-spread between the prices paid by consumers and prices received by growers. It has been estimated that out of every rupee paid by consumers for different commodities, marketing charges amount to 73·6 p.c., in the case of grapes, 57·72 p.c., in the case of oranges, 43·9 p.c., in the

case of tobacco and potatoes, 32·2 p.c., in the case of rice and 31·5 p.c. in the case of wheat.

Remedies : The proposals adopted by the government for remedying the defects in the marketing organisation may be classified into three groups ; *viz.*, establishment of regulated markets, organisation of co-operative marketing, and some miscellaneous measures.

(A) **Regulated Markets :** Such markets were started in 1897 to regulate the sale of raw cotton in Berar. The main outlines of this proposal are the establishment of markets in the main centres of trade where committees are set up to control trade practices and regulate market charges. These market committees consist of the representatives of growers, and traders, and their principal function is to standardise the market practices, reduce charges and to keep watch over the weights and scales in use. Acts have been passed in several States (*i.e.* Bombay, M.P., Madras, Punjab, Mysore and Hyderabad), providing for the establishment of regulated markets. Such markets confer great benefits on the growers. They can get full information regarding the current market prices, which are posted in the market from time to time. They may sell their produce openly, and have not to pay unreasonable market charges. Some of the market committees provide facilities, such as sheds for cattle, godowns etc.

(B) **Co-operative Marketing :** The second step taken by the government is the organisation of co-operative marketing societies. A number of cultivators join together to form such a society, which sells the produce of the members in the market and then distribute the sale proceeds after deducting its own charges. Co-operative marketing has achieved very great success in the U.S.A., and the agricultural countries of Europe.

In India, some progress has been achieved in the organisation of co-operative marketing societies. In 1960-61, there were in all 3108 primary societies, with working capital worth Rs. 28·21 crores. In Bombay, cotton trade on a co-operative basis has been organised throughout the State. Co-operative cotton sale societies numbered 84 in 1949-50 among which there were 11 ginning and pressing societies. Bombay has also started an apex marketing institution in the name of the Bombay State Co-operative Marketing Society for the purpose of co-ordinating the activities of individual marketing societies. In U.P.,

considerable progress has been made in organising co-operative marketing of sugarcane, ghee etc. The sugarcane co-operative sale societies supply 85 to 90 p.c. of the total cane crushed in the factories in the State. Besides marketing case, they have ensured correct weighments to the cultivators, popularised improved varieties of cane and promoted the adoption of improved methods of cultivation. There were also 630 ghee societies in U.P. in 1949-50 with a membership of 17850. These societies purchase ghee from the members and market it at the most favourable prices. The ghee societies are affiliated to central ghee unions which maintain a paid staff to collect ghee. The apex organisation for all co-operative marketing societies is the Uttar Pradesh Co-operative Development and Marketing Federation.

In Madas, Co-operative Paddy Sale Societies have made some progress. There are also co-operative societies for the marketing of fruits, vegetables etc.

In spite of this achievement, the progress of co-operative marketing is not at all satisfactory. The main reasons for such small progress are the lack of efficient men and want of loyalty of the members. Men who possess the efficiency and knowledge necessary for the proper management of a marketing society are not easily found from among the illiterate growers. Secondly, the first essential condition for the success of a co-operative marketing society is that the members of a society should bring their produce to the society. But on many occasions members have not been able to resist the temptation of selling their produce independently whenever the chance rose of getting slightly higher prices. No society can work successfully under such a condition.

There is no doubt that many of the defects in the system of agricultural marketing can be solved by a good co-operative marketing society. Such a society will save the illiterate growers from many malpractices like false weighing, unreasonable market charges, lack of information regarding marketing condition etc. They can arrange for finance by the grant of advances and so prevent the forced sale of crops after harvest. They serve to cut down the number of middle men, and so help in bringing larger incomes to the growers. They may also build godowns or warehouses where the produce may be kept in stock, pending sale in the markets. The government should, therefore, make greater effort to organise the movement as to cover all villages.

(C) **Other remedies** : The government has also undertaken a number of other measures to ensure better marketing of agricultural produce.

(a) *Standardisation of weights* : The central legislature has passed the standards of weights act in 1939 to secure standardisation of weights and measures.

(b) *Grading of crops* : The government has also passed the Agricultural Produce (Grading and Marketing) Act in 1937. Under this Act, the Agricultural Departments undertake to fix the grades of the produce and put their seal as a guarantee of quality. These AGMARK products have become increasingly popular in the country.

(c) *Warehousing* : Following the recommendations of the Rural Banking Enquiry Committee of 1950, a number of States have passed legislation to facilitate the building of godowns and warehouses in important marketing centres. Such warehouses would not only provide storage facilities for keeping the produce in stock ; but they would also serve as a channel for the supply of finance to the growers. The certificates issued by these licensed warehouses can be discounted at the banks and the latter can rediscount them with the Reserve Bank of India.

(d) *Marketing organisation* : The central and the State governments have set up marketing organisations to carry out surveys of the marketing conditions. These marketing officers have carried out important surveys regarding the actual conditions under which different crops are marketed. They have also undertaken the task of grading the produce and issuing the "Agmark" seal. They also help in the development of regulated markets and in spreading correct news regarding prices and stocks, which are often broadcast through the A.I.R.

Recent measures : The Report of the All-India Rural Credit Survey Committee has made a number of recommendations for reorganising the system of agricultural marketing. The Committee felt that if the machinery for the supply of rural credit is to be made effective, it should be integrated with that of marketing. It, therefore, recommended the establishment of a National Co-operative Development and Warehousing Board with two distinct funds under its control. The Board should be set up by statute, and should contain representatives of the differest ministries, the Reserve Bank of India, State Bank etc.

It should be charged with the function of promoting the planned development of the facilities for the storage and warehousing of crops and of the co-operative processing and marketing of agricultural commodities. The Board will have a National Warehousing Development Fund with funds to be contributed by the Government of India. This Fund is to be utilised to subscribe to the share capital of the All-India Warehousing Corporation and to make loans to the State Governments to enable them to subscribe to the share capital of the State Warehousing Companies, or to make loans to these Warehousing Companies. The Act should also provide for the establishment of the All-India Warehousing Corporation with an authorised capital of Rs. 20 crores, to be contributed by the National Co-operative Development and Warehousing Board, State Bank of India, Commercial Banks, Insurance Corporation of India, etc. This Corporation will be entrusted with the function of acquiring and building godowns and warehouses at places of all-India importance, and to run licensed warehouses and to manage regulated markets etc.

The different State governments should also take steps to set up State Warehousing Companies for the purpose of building or acquiring or licensing godowns and warehouses at places other than those earmarked for the All-India Warehousing Corporation etc. The general idea is that while the All-India Warehousing Corporation is to set up warehouses at important centres, the State Warehousing Company will have its godowns and warehouses up to the district and sub-divisional levels, and that in the smaller towns and the taluka head-quarters, Co-operative Societies are to be organised for setting up godowns and warehouses. The State Warehousing Company may encourage such societies by subscribing to their share capital, owing to the high cost of constructing godowns and warehouses, it may be necessary to provide for the grant of a subsidy to such societies.

The government has passed the Agricultural Produce (Development and Warehousing) Act in May, 1956, and the National Co-operative Development and Warehousing (N.C.D.W.) Board has been set up to carry out of the functions enumerated in the Report. One important provision of the Act related to the establishment of the Central Warehousing Corporation, which has been set up in March, 1957. The authorised capital of this Corporation is Rs. 20 crores, divided into 200,000 shares of Rs. 1000 each. Half of this has been issued now, of

which Rs. 4 crores have been subscribed by the N. C. D. Board and the balance by the State Bank, scheduled and co-operative banks, insurance, investment and other financial institutions. This Corporation was expected to set up, during the Second Plan, a chain of about 100 warehouses spread all over India. It will also promote the formation of State Warehousing Corporations, which, in turn, will establish about 250 warehouses at important centres in the States. When these are set up, an important step will be taken to transform the marketing organisation in agriculture.

Questions

1. Describe the present system of marketing of agricultural produce. Point out the defects of this system and show how they can be overcome or mitigated. (All 1931 ; Cal. 1943 ; Punj. 1941 ; Pat. 1957 ; Luck. 1956).
2. Describe the growth of co-operative agricultural marketing societies. Point out the technical and other hindrances in co-operative marketing. (All. 1942).
3. What measures would you suggest for improving agricultural marketing in India ? (Punj. 1953).
4. What are the defects in the present system of marketing of agricultural produce in India ; How can they be removed ? (All. 1953 ; Gau. 1953 ; Bom. 1957).

CHAPTER 14

THE AGRICULTURIST AND AGRICULTURAL LABOUR

The agriculturist : Efficiency of the human factor is one of the most important elements in determining productivity. How far are the cultivators efficient ?

There is a difference of opinion regarding the efficiency of the Indian cultivators. Dr. Voelker spoke highly of the efficiency and careful husbandry of the Indian agriculturist. The Royal Commission on Agriculture also admitted the fact that most of the agriculturists were, more or less, efficient. There is no doubt that most of them possess a good knowledge about the soil conditions and the suitability of particular crops for different types of soil, season etc. This may be readily admitted. But there is no doubt that the average producivity of the Indian cultivator is much less than that of his European or American brother. This is due to a variety of circumstances, over most of which the peasant has no control.

One important reason for such low efficiency is the fact that the Indian cultivators possess ill health and this has sapped their vitality. On account of their poverty, they cannot afford to have good food in sufficient quantities, as a result of which they fall an easy victim to various diseases like a malaria etc. A man in poor health cannot work hard. A second reason is the illiteracy of the cultivators. On account of the lack of education, they do not always get proper knowledge about scientific methods of agriculture. Their improvident and reckless habits are also the result, to some extent, of their ignorance and illiteracy. This lack of ambition and initiative is due to centuries of extreme poverty. Much has been written about their conservatism. But agriculturists all over the world are usually more conservative than the city dwellers. Moreover, time and again it has been proved that when the usefulness of new methods or implements is definitely proved, the cultivators are not slow to adopt them. Part of their conservatism may also be due to the lack of education.

All this points to the supreme need for the spread of the right kind of education among the masses. The peasants must not only be educated in the three R's ; provisions should also be made to teach

them knowledge about the rules of health and the scientific methods of education. Stress should also be laid on teaching them the virtues of thrift and the usefulness of unnecessary expenditure.

Agricultural labour : The term, agricultural labour, is generally intended to include all persons who are hired for carrying on agricultural operations on a permanent or temporary basis. Such persons may or may not own any plot of land which they cultivate on their own account. In fact, there is a large section of petty tenants or sub-tenants, who possess only a fractional area of land which hardly returns enough for the subsistance. These men are forced to work as labourers on the fields of others in order to supplement the meagre earnings from their own land. A close analysis of the census figures of India reveals an increasing tendency of agricultural labour becoming landless. Moreover, the number of such labourers is gradually increasing in the country. In 1882, the census report gave 7½ millions as "landless day labourers" in agriculture, and this number increased to 33 millions in 1931 and to about 44·3 millions in 1951. These are divided into two groups, namely, casual workers and attached workers. Attached workers are those who get work for a month or more at a time, while casual workers, who constitute about 89 p.c. of the total number, are never sure of getting employment for a continuous period.

Conditions of agricultural labour : There is a great diversity of conditions under which agricultural labourers live and work. But all authorities are agreed that their working conditions are worse than those of industrial labour. Industrial labour is better organised in trade unions and other organisations and has, therefore, greater bargaining strength. Conditions of housing amenities, terms and conditions of employment and other measures initiated by the government as well as employees have of late improved the conditions of industrial labour. But agricultural labour is scattered all over the land, and until recently, not much attention was paid to study the conditions under which these workers work and live. Some information has now become available as a result of a series of enquiries made by the Ministry of Labour, Government of India regarding the conditions of agricultural labour in selected villages in different states. These surveys show that a considerable percentage of the agricultural families, from 15 to 40 per cent., consists of agricultural labourers. The average daily wages for these workers were generally Re. 1 to Rs. 1/4/- for men, including the cash

value of perquisities. Woman and children were paid as. 5 to as. 8 in cash or in kind and were generally employed for lighter operations and shorter hours. In the vast majority of cases, the average annual expenditure was larger than the income. According to the official survey, the average annual income per family of agricultural workers varied between Rs. 273·6 in Khuntia (Orissa) to Rs. 641·5 in Brindabanpur (West Bengal) ; while the average annual expenditure varied between Rs. 280 in Khuntia to Rs. 749·0 in Brindabanpur. The expenditure on food was the highest, being more than 80 p.c. of the total expenditure. In spite of that, their diet was poor both in quantity and quality. Majority of them were in debts. The average number of days for which such workers were employed varied between 176 days to 275 days. There is no limit to the hours of work. Hence they suffer considerably from seasonal unemployment, the period of unemployment ranging from 3 to 6 months.

According to the Second Agricultural Labour Enquiry conducted by the Union Ministry of Labour, the average daily wage rate of an adult male worker declined from 109 nP. in 1950-51 to 96 nP. in 1956-57. In the case of women workers, the daily wages rate came down from 68 nP. to 59 nP. during the same period.

Another unfortunate result is that a section of agricultural labourers has been reduced to the status of *de facto* slaves, such as the Hallis in Bombay, the Kamyas in Bihar.

Remedial measures : There is no doubt that the existence of such a large number of agricultural labourers who lack sustained employment is to be regarded as a source of serious weakness and even of instability in the present agrarian system. The Planning Commission have, therefore, recommended a number of steps for remedying this state of affairs. According to the Commission, the Bhoodan movement should be encouraged with special assistance as it provides a means for settling landless workers on land. (*b*) Moreover, block of newly reclaimed land and culturable waste land should be set apart for the settlement of landless workers and of small holders on the co-operative basis. (*c*) Groups of workers should be organised into labour co-operatives and these should be employed extensively for the construction of local irrigation and other works. (*d*) The various governments should provide financial assistance to co-operative groups of landless workers

to enable them to build houses, purchase bullocks and implements and to get training in ancillary industries. (*e*) States should grant special assistance on an extensive scale by way of educational stipends and for vocational and technical training. Lastly, the Minimum Wages Act should be applied to raise wages of these agricultural workers.

Fixation of minimum wages of agricultural labour : The only attempt that the government has made to improve the conditions of agricultural labour is by including it within the scope of the Minimum Wages Act of 1948. Under that Act, the State governments were required to fix the minimum wages for agricultural labour within a period of 3 years. Many State governments have already taken steps to fix minimum wages of agricultural labour. The main difficulty has been the absence of any data regarding the actual wages received by agricultural workers. To stop this gap in our knowledge, the Ministry of Labour conducted enquiries regarding the conditions of agricultural labour in about 2,000 villages. Such sample surveys have been completed.

Even after minimum wages are fixed, the next difficulty will be the proper enforcement of the wages rates. Agricultural labour is absolutely unorganised and wholly illiterate. Moreover, it is scattered over a large area as a result of which organisation of such labour into unions would be difficult. Enforcement of minimum wages becomes almost impossible on account of the lack of trade unions.

Another difficulty will arise on account of the fact that agriculture is not on many occasions a paying proposition in our country. Unless steps are taken to stabilise agricultural prices at a level which will give proper return to the cultivators, fixation of minimum wages will raise more difficulties than it will solve.

Questions

1. Describe the handicaps you know of the agricultural labourers in your locality. What measures would you propose to improve their living conditions? (Punj. 1953 ; Mad. 1953 ; Luck. 1952).

2. Examine the steps that have been taken to regulate the wages of agricultural labourers. Point out the difficulties in the way of such regulation.

3. "At his best the Indian cultivator is as good as any in the world, while at his worst it can be said that his miserable condition is brought about by an absence of facilities for improvement which is probably unequalled in any other country." Elaborate this statement. (Cal. 1941).

CHAPTER 15

SOIL EROSION AND OTHER PROBLEMS

Soil Erosion : The problem arises on account of the fact the surface soil is often wasted by excessive rains or by the flooding of rivers. As a result, large areas of land have become unfit for cultivation. The problem is of special importance in West Bengal, U.P., and Punjab.

There are many factors that are responsible for soil erosion. Under ordinary conditions, the soil cannot be wasted away if there are sufficient trees on the land or if the soil is covered by grass or other green vegetation. So the principal causes of the erosion of soil are (1) the indiscriminate cutting down of trees, and (2) removal of grass or vegetation on account of uncontrolled grazing by goats or cattle. The continuous increasing pressure of population on land has led to large-scale deforestation in order to meet the needs for fuel. The consequence of such deforestation is that the soil is left unprotected and gets washed away during heavy rains or flooding. Cultivation on the slopes of hills has also been known to result in soil erosion.

Soil erosion results in serious evils. In the first place, the first few inches of the surface soil are a store of nutritive chemicals and organic matter. Loss of this matter reduces the productivity of land. Secondly, as soil erosion proceeds, the land gets drier, and on account of the absence of such windbreaks as trees, bushes, hedges and grass, the area becomes more liable to storms of dust and sand. All these results do not occur within a year or two. But in course of decades, soil erosion would lead to abandoned regions, run-down communities, and wandering agriculturists. No wonder that soil erosion has been regarded as "creeping death."

The main remedy against the evils of soil erosion is to be found in a policy of afforestation. The trees of the forest protect and conserve the soil. Their roots and the grasses check the flow of rain or flood water and thus help seepage. They hold together the soil particles tightly and thus prevent soil erosion. Secondly, the practice of uncontrolled grazing should be controlled. A third way is to adopt the method of cantour cultivation on the plains. Bunding at small distance across the

sloping fields should also be adopted in the place of the present system of bunding at the bottom of the field.

The Planning Commission have recommended a number of steps for organising appropriate soil conservation measures. Each State should, in their opinion, pass the necessary soil conservation legislation. It should also carry out a survery for the demarcation of the main areas affected by erosion and then adopt proper remedies for soil conservation. The government has already established a research station at Jodhpur to study the problem of checking the advance of the Rajasthan desert. Already good results have been obtained in this connection by the adoption of the policy of creation of vegetation belts.

Soil deterioraion and manuring: Another problem is the danger of the exhaustion of the soil in India. Estimates of the yield of crops published from time to time show that there has been a decline in the yield per acre. This declining trend has given rise to the question, whether the soil of India is getting exhausted or not. As early as 1893 Dr. Voelker raised this question in his report and pointed out that though there was no positive evidence of soil exhaustion, careful observers were, however, afraid of such a fact. The Royal Commission on Agriculture writing 35 years after Dr. Voelker, also drew attention to the difficulty of determining the question on account of the paucity of data over any long period of time. The Commission concluded that a balance had been established and no further deterioration was likely to take place under existing conditions of cultivation.

Whatever the actual state of soil exhaustion, the presumption is that the fertility of the Indian soil is declining. There are good reasons for such expectation. It is well-known that what is removed from the soil in the form of crops should also be restored to it in some other form. Continuous cultivation of land is bound to reduce fertility unless manure is given to land in proper proportions. On account of poverty and certain other factors, only a small amount of manure is applied by the cultivator to his land. The most readily available manure, cowdung, is burnt as cakes on account of the non-availability of cheap fuel. Prejudices stand in the way of the use of fish or bone. Oil-seeds were, until recently, exported and so we lost the oil cake. Hence our farmers could use only small quantities of manure.

The question of the application of manure is of highest importance for increasing the yield from land. But unfortunately the supply of manure is extremely inadequate in this country. The usual sources of manure are cow-dung, green manuring, bones and fish, night soil, oil cakes and chemical fertilisers.

Cow-dung : It is the most commonly available manure in the villages whose cattle population numbers about 200 millions. Unfortunately this is burnt as fuel by the cultivator as generally they have nothing else they could use as fuel. The urine of the cattle, which may also be used as manure, is usually allowed to go to waste. This is a great loss. The only way of stopping this suicidal practice is to provide alternative sources of supply of fuel. Quick growing trees should be planted round the villages to provide cheap fuel for the cultivators. Villagers should also be taught to dig pits for preserving manure.

Green manuring : This is one of the most important methods for restoring organic matter to the soil. Leguminous crops are grown and ploughed back into the soil before the next food or cash crop is grown. Such crops increase the humus and nitrogen content of the soil. They also protect the soil against erosion. The Indian cultivator knows the value of this method and what is now necessary is for the government to carry on an intensive propaganda in favour of green manuring and to distribute seeds of these crops among the cultivators.

Bones and fish. These serve to fertilise the land as they supply nitrogen to the soil. But on account of social prejudice, these are not much used by the cultivators. Such prejudice dies hard and this is a great difficulty.

Night soil : It is a valuable manure, which is unfortunately not used in our country on account of the prejudices of the cultivators. Some municipalities have begun to manufacture poudrettee from night soil. In the villages trench latrines can be dug for composing human excreta. This will provide manure and improve the sanitation of the villages.

Oil cakes : Oil cakes which remain after oil are crushed from the seeds of cotton, groundnut, mustard etc., are a valuable source of nitrogen. Unfortunately these oil-seeds were exported to foreign countries, as a result of which oil cakes were lost. Recently we have begun to manufacture oil in our country. A good deal of propaganda should be carried on to popularise the use of this form of manure.

Chemical fertilisers : In the western countries manure is supplied to land in the form of sulphate of ammonia, nitrate of soda etc. These had to be imported from foreign countries and were also expensive. Recently the Government of India has set up a factory at Sindri in Bihar for the manufacture of artificial fertilisers. Production has already been started in this factory and it is expected that we would become self-sufficient in this respect within a near future.

The cattle : The importance of cattle arises on account of the fact it provides the only motive power in agricultural operations. In western countries horses were used in ploughing land, and are now being replaced by machines. Cattle are valued mainly for their meat and milk. But in India cattle are used for ploughing land, for transporting the produce and lastly, for providing milk. The importance of the cattle is, therefore, greater in our country than in the west.

In spite of the importance of the cattle, there are certain disquieting features in regard to our cattle population. In the first place, the total number of cattle is very large as compared to the needs of tillage. It has been estimated that we have about 100 cattle per 100 acres of cultivated land as against 38 cattle in Holland and 25 cattle in Egypt. Secondly, a large number of cattle in India are old and decrepit, and constitute a great burden on an already impoverished land. This is due to the prejudice among the Hindus against cow-killing. Moreover, there is a vicious circle of excess numbers and poor quality. The worse the quality of cattle, the greater becomes the need for having larger numbers. As the number of cattle increases, the pressure on the available supply of fodder leads to poor health and small strength in the cattle. As cattle grow smaller in size and poorer in health, farmers are forced to breed more and more cattle. The vicious circle goes on in this way. Thus we find in the country large numbers of weak, small-sized cattle and this involves a serious drain on our scanty fodder resources.

Improvements in livestock : The necessity to improve the quality of cattle arises not only on account of their usefulness in agricultural operations, but also for increasing the supply of milk in the country. Milk is one of the most important protective foods. It has been rightly said that the health and the intelligence of children depend largely on the quality and amount of milk, consumed by them. Unfortunately, the per capita consumption of milk is extremely low. It does not on the average exceed six to seven ounces per head per day. This is due

to the large numbers of people in our country and to the fact that the annual production of milk per head of cattle is very low. While the annual production of milk per head of cattle in India has been estimated to be 30 gallons, it is 389 gallons in Denmark, and 326 gallons in Sweden etc. We must, therefore, take steps to improve the quality of cattle so as to get more milk.

Three things are necessary to improve the quality of cattle,—better feeding, better breeding and better veterinary arrangements.

Cattle diet : Like their owners, Indian cattle are also underfed on account of the inadequate supply of fodder and other articles of cattle diet. Several steps may be suggested to improve the diet of the cattle. Investigation has shown that a mixture of oil-cakes, bran, barley and gram husk provides a good protective food. Fortunately the production and supply of oil cakes are increasing on account of the growth of the oil pressing industry in the country. In order to increase the berseel and other grasses and fodder, attention should be paid to conserve the pasture lands and to control grazing during the monsoons so as to increase the yield of grass. Wherever it is possible dual purpose crops like jowar, bajra, millets and pulses should be introduced. These will provide additional fodder.

Better breeding : The stock of cattle has deteriorated on account of indiscriminate breeding. To improve breeding, three steps are necessary. First, better breeds of cattle ought to be popularised by organising cattle shows etc. Secondly, arrangements should be made for making better breeds of bulls available for the purpose of cross-breeding on easy terms. Lastly, undesirable bulls should be prevented from breeding.

Cattle diseases : For curing cattle diseases, larger numbers of veterinary hospitals should be opened all over the country. Doctors from these hospitals should visit the villages from time to time. Veterinary Departments should carry on research to find out cheap medicine for the various diseases from which cattle suffer.

Questions

1. What do you mean by soil-erosion ? Describe the economic effects of soil-erosion and suggest some measures for tackling the problem.

2. Examine the livestock problem in India. What would you suggest to meet the defects ? (Mad. 1953).

3. Account for the poor quality of Indian cattle. What steps have been taken by the Government in recent years to improve our cattle wealth ? (Bih. 1953).

CHAPTER 16

LAND TENURES AND ZEMINDARI ABOLITION

In the discussion of the causes of low productivity in agriculture, it has already been noted that the system under which land is owned and cultivated in India is also an important contributing factor. There are two allied problems—the problem of land tenure, *i.e.*, the legal or customary system under which land is owned, and the problem of land tenancy, *i.e.*, the system under which land is actually cultivated and the product divided between the owner and the cultivator. In a study of the systems of land tenure, we discuss mainly the question of ownership, sale or mortgage of land. Land tenancy is concerned with the study of the question of security under which cultivators hold land and the division of the product.

The importance of a study of the system of land tenure will be obvious from the following quotation from a report prepared by the UNO on Land Reform. The land tenure system "may reduce the standard of living of the peasant by imposing on him exhorbitant rents or high interest rates ; it may deny him the incentive or the opportunity to advance and it may check investment because it offers him no security. It may lead to the prevalence of farms which are too small to be efficient units of production or too large to cultivate intensively."*

Systems of land tenure : The systems of land tenure prevalent in India may be divided into three broad groups, *viz.*, the ryotwari system, the mahalwari system and the zemindari system.

In the *ryotwari system of tenure*, land is held by the cultivators directly under the State. There is no landlord or any other intermediary. Cultivators pay rent directly to the government at rates determined by the latter. They can sub-let their land or transfer or mortgage it. The rates of rent to be paid by the cultivators are revised at the time of settlement operations which take place usually at the end of 30 or 40 years. In the large majority of cases, owners themselves cultivate the land. But in cases of large holding, a portion is let out to tenants. This system prevails in Bombay, Madras, Assam, and parts of Punjab.

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* *Land Reform. Defects in Agrarian Structure as obstacles to Economic Development.* United Nations. 1951. P. 5.

In the *mahalwari system of tenure,* land is held jointly by co-sharing bodies of villagers or village communities. The government has recognised the rights of ownership of such bodies. The whole estate is assessed by the government to one sum of land revenue, and all members are jointly and severally responsible for the payment of land revenue. In Punjab, the government recognises one of the members of the village community as the headman who is called the lambardar. The system prevails in Punjab and U.P. In the former State owners themselves cultivate the land, while in U.P., cultivation is usually done by a class of tenants.

In the *zemindari system of tenure,* land was owned by the landlord who was responsible to the government for the payment of revenue. Actual cultivation was carried on by tenants who hold land under landlords. There were two different types of zemindari tenure. In the first type, known as the permanent settlement, the revenue to be paid by the landlord was fixed in perpetuity and could not be increased by the government. The landlord was, however, free to raise the rent to be paid by his tenants. This system prevailed in West Bengal, Bihar, Orissa, parts of Madras and Assam and U.P. In the second type of zemindari system, the revenue to be paid by the landlord was revised from time to time. This system prevailed in Oudh and Agra in U.P., and in M.P. In Madhya Pradesh, the government found a number of persons who were originally farmers of taxes under the Marathas and who claimed the rights of a landlord. They were recognised as landlords by the government and were known as *malguzars.* The revenue to be paid by the malguzars is revised periodically. The system is also known as the *malguzari system.*

Merits and defects of these systems : Very few people now-a-days find any merits in the zemindari system as it prevailed before. Under the ideal zemindari system, the landlord lives in the village, invests large sums of money on the improvement of land and places his knowledge of scientific agriculture at the disposal for his tenants. But in the zemindari system which prevailed in India, very few landlords lived in the villages and took care to invest money on land improvement. They lived in the cities and their agents and officers oppressed the tenants in various ways. In West Bengal and other areas where the land revenue was fixed permanently, the State was losing large amounts of revenue.

The general opinion is in favour of the ryotwari system of tenure. The great merit of this system is that it puts the cultivator in direct touch with the State. Since the cultivator is himself the owner of land, he will have every incentive to cultivate his land properly. There is no landlord to take a share in the product. It is of course true that in some areas owners of large holding have sub-let their land to tenants, as a result of which the tiller of the soil is not its owner. But this has not become a serious problem as yet. A second advantage of the ryotwari system is that it may encourage the government to invest money on land improvement.

The ryotwari system has, however, a number of defects. In the first place, the periodic revision of land revenue at the time of each settlement operation may exercise unsettling effects on the cultivators. The provisions for a revision of land revenue leave a good deal of discretion to the settlement officers. There is necessarily a great deal of guess-work in the process of evaluation of these factors. As a result, assessment of land revenue has often been arbitrary and gave rise to much discontent among the ryots.

The mahalwari system is more or less similar to the ryotwari system in its effects on agricultural operations. In so far as the owners of land actually cultivate it, we are able to secure the benefits of peasant proprietorship. If, however, land is let out to tenants who are the actual cultivators, the system is likely to exercise an adverse effect on agricultural production.

We have yet to find out the ideal system of land tenure under which the conditions of ownership of land will promote, instead of hindering agricultural improvement and enable the vast majority of farmers to enjoy a higher standard of living.

Principles of assessment under the ryotwari system : In the ryotwari system, the government fixed the revenue to be paid by each owner of land at the end of a number of years. The system was first introduced in Madras and had generally been extended to other States. Though the system as adopted in different States is, in essentials, the same, there are some differences with regard to the principles of assessment. In Madras, the first step in the process of assessment is the preparation of what is called the cadastral record. The settlement officers visit different villages and carry out a classification of soils

according to their productive capacity. Experiments are then carried out on different classes of soil to determine their normal yield. The next step is the determination of the value of the estimated amount of crops on the basis of the average of the prices prevailing in the last 20 years. In this way the value of the produce on each class of soil is determined. From this gross value, deductions are made on account of the estimated cost of production including costs of transport. The sum that remains is the net profit from each acre of land on different classes of soil. Not more than 50 p.c. of the net profits is to be fixed as the land revenue. This is how the original assessment was made. Re-assessment is made at the end of every 30 years, when the amount of land revenue is raised or lowered, depending on the extent of the change in average prices over the last 20 years. Whatever the rise in average prices, revenue cannot be enhanced beyond 18¾ per cent of the old demand.

The principles of assessment are nearly the same in Bombay. But in Bombay revenue is assessed on the basis of the purpose for which land is used and on the basis of the kind of crops grown on land. Moreover, at the time of re-settlement, changes in the land revenue demand are made, not on the basis of average prices, but on general economic considerations.

Principles of assessment under the mahalwari system: The method followed in fixing the land revenue is similar in many respects to that under the ryotwari system. In Punjab, the settlement officers undertake a survey of all land in the villages, classify the soil, and determine the average yield from each class of soil. The next step is the determination of the money value of the gross produce on the basis of average prices. Out of this sum the officers determine the net produce or net assets as being equal to the rent, or that portion of the gross produce which would have, if the land were rented, been taken by the landlord. The share of the government is fixed generally at one-fourth of the net assets. In U.P., the share of the government is normally fixed at 40 per cent of the net assets. Re-settlement takes place at the end of every 40 years when enhancement of rent is limited to one-third of the previous amount.

Principles of assessment under the permanent settlement: In the permanently settled areas, the government recognised the zemindars as the proprietors of the estates held by them, subject to the

regular payment of revenue. The system was introduced by Lord Cornwallis in 1793, when the revenue to be paid by each zemindar in respect of the land held by him was fixed at ten eleventh of the estimated amount of rent received by him. This amount was fixed in perpetuity and was not to be enhanced under any circumstances. The zemindars were, however, free to charge any rent to their tenants. The government laid down only two conditions. First, if the land revenue is not paid by the due date, the estate would be sold in auction for the repayment of the arrears of revenue. Secondly, the government reserved the right to introduce legislation for the protection and welfare of the tenants.

Merits and demerits of permanent settlement: The permanent settlement of land revenue was introduced in Bengal, Bihar and Orissa in 1793. At that time, the East India Company was not sure of its hold in India and had to spend large sums of money in financing a number of wars fought in India. The introduction of the system of permanent settlement was thus of great benefit to the company. The company was assured under this system of getting a definite sum of money as land revenue, without bothering about the actual administration of the country. Moreover, zemindars, who were granted full rights of proprietorship, had every reason to support the administration of the company. They became loyal supporters of the British, and this was an important factor in stabilising the British rule in India. Lastly, Lord Cornwallis was actuated by a good motive in introducing this system. He was himself a member of the British landed aristocracy, and thought that the system of landlordism would confer great benefits on this country as well. The zemindars, like the British landlords, would invest money on land improvement, and so would benefit everybody connected with land.

The benefits of this system to the East India Company are not doubted by any writer. But in course of time the results of this system were found to be unsatisfactory, and so even the East India Company decided against the introduction of this system when, one by one, other provinces came under its administration. The government, no doubt, obtained fixed and stable revenue from land without being forced to maintain a large staff for the assessment and collection of revenue. But as against this benefit, we must put the loss of revenue which the government have suffered over decades on account of the fixity of

land revenue. As conditions became settled in the country, the level of rent increased considerably, aided by the growth of population and the rise in prices. The benefits of higher rents were pocketed entirely by the zemindars, and the government had to remain content with fixed amounts of revenue.

The perpetual fixity of land revenue had other consequences. In the first place, different governments felt no inducement to invest capital on land improvement, since the benefits of such improvement would be enjoyed only by private landlords. Moreover, zemindars belied Lord Cornwallis's expectation, and did not invest much capital on their land. They began to live a life of luxury in the cities, leaving the management of their estates to paid servants.

A second consequence has been the fact that governments lost all contact with the rural areas as they did not consider it necessary to maintain the staff for that purpose. The interests of the cultivators suffered as a result. Cultivators also suffered in other ways. In the ryotwari areas, the government usually granted remissions of land revenue in areas suffering from a failure of crops due to drought or flood. But in the permanently settled areas, the land revenue was fixed for all time and the government insisted on collecting the full revenue from zemindars in all years, good or bad. The zemindars, in their turn, collected their rent from royts even in years of drought or flood. The lot of the cultivators living in permanently settled areas thus became worse than that of their brothers in ryotwari areas.

Cultivators suffered on another account. In order to enable landlords to pay the revenue in time, the government passed a series of regulations in their favour. Zemindars took advantage of them and began to ignore all the customary rights of the ryots. As the growth of population raised the demand for land, zemindars began to charge high rents. In consequence, ryots were rack-rented.

The burden of rents on the ryots increased on account of the growth of sub-infeudation which was a consequence of the system of permanent settlement. With the rise in the level of rents, the margin between the fixed land revenue and the total rent began to increase. This enabled the zemindars to divide their estates and to lease these parts to other men at higher rates of revenue. A large number of middlemen (like Pattanidars, Talukdars, Jotdars) grew up between the zemindars and the

cultivators. In some cases there were as many as 50 or 60 such intermediaries. As they were mostly rent-receivers, their sole interest lay in increasing the level of rents as much as possible. This meant increasing burden on the ryots.

As has already been stated, one deplorable consequence of the system of permanent settlement was that land became nobody's concern. The zemindar became a mere rent-receiver and ceased to take any interest in land. The large number of middlemen who flourished between the zemindar and the ryot were interested only in collecting as high a rent as the conditions permitted. The cultivator had no money and often no incentive. The government lost all interest as the land revenue was fixed in perpetuity. As a result, nobody felt any responsibility for the best use or improvement of land.

The system of permanent settlement exercised an adverse influence not only on the growth and improvement of agriculture, but also on other aspect of the economic organisation of the country. On account of the fixity of land revenue, purchase of a zemindari estate became a highly profitable proposition. In addition, ownership of a estate conferred great social prestige. Hence men, who possessed surplus money, invested it in the purchase of zemindari estates. The system was, therefore, indirectly responsible for checking the growth of industries by diverting capital from investment in industries where the returns were uncertain, to landed estates where profits were quick and sure.

It has, however, been urged by a number of writers that the system of permanent settlement conferred an important benefit on the country in an indirect way. It has given rise to the middle class, whose members have been responsible for bringing about social, literary and educational advancement of Bengal. But Bombay, which is a ryotwari area, has also a prosperous middle class. Hence the growth of a middle class cannot be ascribed to the system of land revenue. The late R. C. Dutt claimed that one consequence of the limitation of the demand for land revenue was that the peasants of Bengal enjoyed on the average greater prosperity than their brothers in other areas. But if the Bengal peasant is comparatively more prosperous, this is due, not to the permanent settlement, but to the greater fertility of land and to abundant rainfall in Bengal.

There is, therefore, no doubt about the fact that the system of permanent settlement produced obstacles to the progress of the country. Mere reform of the system is not enough. There is no justification, whatsoever, for retaining the system or for preserving 'landlordism'. The Congress have rightly adopted the proposal for the abolition of the zemindari system, and this has already been carried out in almost all States including West Bengal.

Abolition of zemindari estates : Whatever the justification of the system in the early days of the East India Company, there is no doubt that the system produced great obstacles to the progress of the country. It fixed the revenue from land, involving the State in considerable loss of revenue and so deprived the government of close contact with agricultural conditions. The ryots suffered in many ways. They lost all customary rights, and were forced to pay an ever-increasing rent, due to some extent, to the pressure of population, and to the growth of a large number of middlemen between the zemindar and the ryot. The country has also suffered materially. On account of this system, land became nobody's concern. Cultivators, being poor, had no money to invest. Zemindars ceased to invest and the government did not feel any desire to invest in land. Lastly, the system had been responsible for diverting surplus capital from investment in industries where the prospects of profits were uncertain into the purchase of landed estates. It has, therefore, indirectly put obstacles to the development of industries.

The general opinion of the country is rightly in favour of the abolition of the zemindari system. It was a part of the Election Programme of the Congress, and appropriate legislation has already been passed in almost all States for the abolition of the system. In West Bengal, the Government has passed an Act to this effect in 1953.

The zemindari abolition acts : All these Acts for the abolition of the zemindari system follow, more or less, the same pattern. The government is authorised to fix a particular date, after which the rights of landlords, malguzars, talukdars, jagirdars, pattanidars and all other tenure-holders will vest in the government. While the number of large estates is not very large, the number of zemindars and intermediaries is not so. In U.P., for example, their number goes up to about 23 lakhs. Most of them owned small estates. The ex-zemindars will continue to

own their home-farms, buildings and other properties like private tanks and enclosures etc. The term, home-farms, generally refers to the land that is registered as *Sir* or *khudkasht* or private land, whether personally cultivated or not. In Madras and U.P., home-farms must be personally cultivated. In addition to the landed estates, the Acts also seek to take over forests, fisheries, waste lands as well as mines and minerals. Private *waqfs* and trusts are also to be taken over. But religious, educational and charitable institutions have been given favourable treatment, and attempts have been made, as far as possible, to keep up their present incomes.

After the estates are taken over, the State governments are to prepare compensation rolls in accordance with the prescribed procedure. It should be noted that under the Indian Constitution, payment of compensation is obligatory whenever any private property is taken over by the State. Provisions for the determination and payment of compensation vary in different States. Rates of compensation are fixed on the basis of 8 or 10 times the net incomes from each estate. This sum is to be paid partly in cash and partly in non-negotiable bonds maturing in 20 to 30 years.

It has been estimated that the total amount of compensation to be paid in seven States *viz.*, Assam, Bihar, Madhya Pradesh, Madras, Orissa, U.P., and West Bengal, would be Rs. 414 crores. As a result of the abolition of this system, these seven State governments will receive in all an additional annual revenue calculated at the Rs. 19·52 crores, *i.e.*, about 4·7 p.c. of the total compensation.

Effects : The abolition of the zemindari system has freed India's land system from the clutches of a feudal system of land tenure. It is, of course, true that the mere abolition of zemindars does not confer any immediate benefit on the tenants. The tenants do not gain any new rights under these Acts, nor are their rents reduced in any way. Everywhere they will have to pay rent at the same rate as before, excepting those fortunate few who will be able to buy their holdings. Of course if there are no zemindars, tenants will not have to pay *abwabs* or illegal cesses. Though the tenancy Acts declared these exactions as illegal, tenants were on many occasions forced to pay these to the zemindars or their agents. As against this we must consider the fact that the place of these zemindars or their agents may be, and will

probably be, taken by the revenue officials of the government, whose corruption is well-known.

Though there may not be any immediate gain for the tenants, they are likely to be benefitted in the future. One result of the abolition of zemindaries will be the simplification of the tenancy system. The tenants will be brought directly in touch with the government and will gain an independent status. There will be an important psychological gain because of the fact that the domination of one class over others will cease. With the state as landlord the tenants will enjoy greater security of tenure.

The problem of payment of compensation : The question of the payment of compensation has given rise to a good deal of controversy. Since the Indian constitution makes the payment of compensation obligatory, all the Zemindari Abolition Acts have provided for the payment of compensation. The basis for the determination of compensation is, of course, different in different States. In Assam, Bihar, Madhya Pradesh and Orissa, the basis is the 'net income' from each Zemindari ; in U.P., it is the 'net assets', and in Madras, 'the basic annual sum'. The basis of net income and net assets is the same, and is to be determined by deducting from the gross income of the Zemindars such sums like land revenue, cess, agricultural income tax, cost of management and costs of works of benefit to the ryots etc. The cost of management is to be fixed on different principles in different States. The rates of compensation including rehabilitation grants vary from 8 times (in the case of estates of large income) to in U.P., from 3 times to 20 times in Bihar and Orissa ; and from 4 to 15 times in Assam. In these States, in calculating the net income, the present income from the estate is taken into consideration. But in Madras, the amount of compensation was to be related, not to the 28 times (in the case of estates of lowest incomes) the annual assets present income, but to what 25 p.c. of the land revenue demand would be after the ryotwari system was introduced in those areas. The 'basic annual sum' is to be determined after deducting from one-third of the gross annual ryotwari demand, 5 p.c. of the demand on account of establishment charges etc., and $3^1/_3$ p.c. on account of maintenance of irrigation works. The rates of compensation vary from 12½ times to 30 times the basic annual sum. It has been estimated that the total amount of compensation to be paid in 7 States would be Rs. 414 crores.

Different methods for paying compensation have been adopted in different States. In Bihar and Orissa, compensation may be paid in cash or in bonds or partly in cash and partly in bonds. These bonds will carry interest at 2½ p.c. with a maturity of 30 years. In Madras, payment is to be made in cash in one or not more than 5 instalments. In U.P., compensation is to be paid in the form of non-negotiable bonds of 40 years' maturity, carrying interest at 2½ p.c. with a maturity of 30 years. In Madras, payment is to be made in cash in one or not more than 5 instalments. In U.P., compensation is to be paid in the form of non-negotiable bonds of 40 years' maturity, carrying interest at 2½ p.c.

Two questions were debated in connection with the payment of compensation,—the financial implications and the justice of the payment. As regards the financial implications, it has been recognised that compensation was to be paid either in cash or in bonds. The total compensation was estimated to amount to Rs. 414 crores. If the whole sum was to be paid in cash, it would be impossible for the States to buy the zemindaries. Most of the States were running deficient budgets, and their resources would be entirely insufficient for the payment of cash. They might borrow the amount from the Government of India. But the latter already expressed its inability to give financial assistance to the States for this purpose. A second way to raise cash was for the States to borrow from the money market. But the conditions in the Indian money market were so depressed that it would not be possible to raise such a large sum from the market. So the States had no option but to pay the compensation in bonds. But if ordinary, negotiable bonds were issued, these might be sold by the zemindars in the market, and such a large-scale sale of bonds would disorganise the market for government securities. It had, therefore, been decided to pay compensation in the form of non-negotiable bonds to all but the small zemindars.

Mention should be made in this connection of one interesting experiment made by U.P. Government to raise funds for the payment of compensation. The tenants were encouraged to become *Bhumidars* or owners of their land and by paying 10 times their rent into a seperate fund, known as the Zemindari Abolition Fund. A *Bhumidar* would enjoy transferable rights over their land and would have to pay 50 p.c. of their existing rent as land revenue to the government till the next

settlement which would take place after 40 years. The same method has been adopted in Madhya Pradesh. But in spite of the intense propaganda, U.P. Government succeeded in collecting only Rs. 32 crores.

The justice of any payment of compensation has been attacked from many sides. A large section of the people have regarded the payment of any compensation as being unnecessary on account of the fact that landlords are mere functionless intermediaries. The majority of landlords have exploited and rack-rented the tenants for such a long time that they do not deserve any compensation. Others point to the fact that many landlords had played a very reactionary role in the movement for the freedom of our country. The payment of proper compensation would only perpetuate the heavy financial burden of the zemindari system. While there is a great force in these arguments, it should also be remembered at the same time that many of the present-day landlords are individuals who have made genuine investments in land for which they deserve some compensation. Land is but one form of property, and it is a wrong principle to penalise one form of investment. The great bulk of the middle class people of our country depend to a great extent on the income from zemindari estates. It is only an act of simple humanity to pay some compensation in order to enable them to start on a new career of usefulness.

Questions

1. On what grounds is the abolition of the Permanent Settlement desired ? What would be the probable effects of its abolition on the economy of the country ? (C.U. 1950 ; Pat. 1953).

2. How far has the object of bringing about radical land reform been achieved by the abolition of zemindari ? (Bom. 1957).

3. What is the difference between the 'zamindari' and 'ryotwari' system of land tenure ? How have they been affected by recent land reforms ? (Del. Hons. 1959).

CHAPTER 17

THE REFORM OF THE LAND TENURE

The problem of land reforms : The abolition of the zemindari system is only a beginning. It has resulted in the removal of an important obstacle to the introduction of land reforms. The abolition of the zemindari system has not solved the problems of land tenure. The Zemindari Abolition Acts have introduced certain changes in the system of land tenure. They have often resulted in the simplification of the tenancy system. In the place of a large variety of rights and tenures, there is now a comparatively small number of tenants and owners. These Acts have enlarged the number of tenants who would be able to acquire land, and thus become landowners. Moreover, the tenants have been brought into direct relationship with the State. The State now occupies the position of the landlord, fixed and collects land revenue and maintains the necessary records. These are, no doubt, desirable changes. But they do not solve the land problem. Time has now come to consider the adoption of schemes of re-organisation so as to increase the yield from land and to secure social justice for all.

Principles of land reform : What are the principles according to which the systems of land tenure found in different parts of the country are to be reformed? The first consideration is that the system of land tenure should be such as to encourage the maximisation of output from land. Indian agriculture has for long remained in a stagnant condition and part of the responsibility for such a state of affairs must be laid at the door of the systems of land tenure. Too often these have resulted in killing the initiative of the cultivators. Hence it is necessary to carry out reforms in such a manner that the system of land tenure should not only provide any impediment to the adoption of improved methods of cultivation, but should provide a great incentive to the increase in production. This means that the measures of land reform should eliminate exploitation, and provide security for the tenants and the workers. Secondly, while it is no doubt imperative to raise agricultural output as much, and as early as possible, we should also remember that agriculture is a way of life. Hence proposals for land reform should also be such as to favour the organisation

of a broad-based social structure in the rural areas. In the words of the Planning Commission, "the land policy should be such as well reduce disparities in wealth and incomes,......and promise equality of status and opportunity to different sections of the rural population." It is this factor which has prompted the Commission to advocate the fixation of ceilings on land holdings and the redistribution of surplus lands among the landless cultivators. It means that whatever the arguments in favour of large holdings these have no place in the Indian economy as they would increase the inequalities of income and wealth in the rural areas.

One or two other factors should also be taken into consideration. For example, the land policy must also fix a floor to land holding and no holding is to be allowed to fall below this size by transfer, sale or gift. Hence some restrictions on the right to transfer land freely should also be included in the land policy. A good land policy should be based on large-scale peasant proprietorship, fixation of fair rents and a more or less permanent and heritable ownership, with restrictions on both the minimum and the maximum sizes of holdings.

Proposals of land reform in the Five-Year Plans: The Planning Commission have correctly stated that the future of land ownership is perhaps the most fundamental issue of national development. Their proposals for land reform may be classified into several heads; (*a*) intermediaries, (*b*) large owners, (*c*) small and middle owners, (*d*) tenants-at-will, and (*e*) landless workers.

The first step is the abolition of all intermediary rights including the zemindari system. This has been done in almost all States. This should be followed by the organisation of an efficient system of revenue administration. As the information regarding village records was often inadequate, steps were taken to undertake a special census of land holdings and cultivation in all States.

With regard to large owners, the Commission have recommended that an upper limit for land may be fixed for (1) resumption of land for personal cultivation and (2) future acquisition. Where land is managed directly by large owners, there should be an upper limit to the amount of land which each individual may hold. This limit should be fixed by each State in the light of several criteria *viz.*, the amount of land revenue paid, the value of the gross produce of land, value of

net produce or income of land. Broadly speaking, an upper limit equal to 3 times a family holding (defined as including that amount of land which a family of average size working with such assistance as is customary in agricultural operations is able to cultivate) may be regarded as a fair limit. Land in excess of this upper limit is to be taken away from existing owners and redistributed among others. The fixing of such an upper limit has been justified mainly on grounds of social justice. As excessive concentration of wealth is not considered desirable, so also concentration of landed property above a certain limit is also undesirable, especially in view of the shortage of land as compared to the rural population. But against this should be set the consideration that such a step may hamper large-scale farming with up-to-date appliances, and may lead to a decline in agricultural efficiency.

As regards small and middle owners, the general aim should be to encourage and assist them to develop their production. The small owners should be encouraged to consolidate their holdings and to organise themselves in co-operatives.

The tenants-at will should be given security of tenure, and should be asked to pay fair rents. In fixing fair rents, the main consideration should be that, having regard to the expenses of cultivation and other risks, a fair wage remains for the cultivators. As far as possible, rents should be reduced to one-fourth or one-fifth of the produce.

As regards the landless workers, the problem is, of course, difficult of solution. The fixing of an upper limit to land-holding and the consequent redistribution of excess land among these classes may bring some relief. But this will touch only the fringe of the problem. The Commission expressed the opinion that Acharya Vinoba Bhave's land gift movement should be supported through special assistance, and such gifts should be made a permanent feature of rural development. Blocs of newly reclaimed land as also cultivable waste land should be set apart for the settlement of landless workers on co-operative lines.

The abolition of intermediaries and the fixing of an upper limit to land-holding are negative achievements. They do not contribute much to promote agricultural development. A real and lasting solution can only come through the organisation of co-operative farming and ultimately of co operative village mangement in which land and other resources of a village can be managed and developed so as to increase

and diversify agricultural production and to provide non-agricultural employment.

Tenancy legislation : In zemindari areas and to a large extent in the ryotwari areas, owners of land have let out either the whole or part of their holdings to tenants who actually carry on cultivation. The pressure of population on land and the absence of other occupations in the rural areas have led to a considerable increase in the number of such tenants. The growing poverty of these cultivators and the oppression and rack-renting of tenants gave rise to considerable agrarian discontent and the State in India has been forced now and then to enact tenancy laws to protect the interests of tenants.

The central aim of these tenancy laws, which varied in details in different States, was to ensure fixity of tenure and fair rents for the vast majority of tenants. Tenants were generally divided into two groups, *viz.*, occupancy tenants and non-occupancy tenants. Occupancy tenants were granted the right to occupy the land held by them permanently subject to the payment of rent. Their holdings are heritable and transferable. Though the rent paid by them is fixed by custom and usage, it can be increased only under certain given conditions and at a given rate. The position of non-occupancy tenants is, of course, inferior. They do not enjoy the same security of tenure, and their holdings may not be transferable.

In addition to these two groups of tenants, there is a third group known as *bargadars, adhiars* or crop-sharing tenants. These are tenants at will and cultivate land on a crop sharing basis, instead of on the basis of fixed money rent. They do not enjoy any security of tenure, though they are usually left undisturbed so long as they continue to pay their high rents. Attempts are being made in recent years to confer some rights on these people.

In recent years a series of Act have been passed in different States in respect of tenants. The general policy has been to enable tenants to become owners of land held by them. The Bombay Tenancy and Agricultural Lands Act of 148 seeks to confer permanent tenancy rights on certain groups of tenants and to give them the status of protected tenants. Tenants who have cultivated land personally for 6 years prior to January 1938 or January 1945 will be recognised as protected tenants. The burden of proof, whether a tenant is protected

or not, lies on the landlord. A protected tenant has been given the right (*a*) to purchase a holding of a maximum size of 50 acres at reasonable prices, (*b*) to exchange his holding with another protected tenant in the same village, (*c*) to erect farm-houses and (*d*) to get compensation for improvements made by him on eviction. His tenure is permanent and heritable, and he can be ejected only on specified grounds. In case of ordinary tenants, their tenure has been fixed at 10 years at a time, and if the tenant is allowed to remain in possession after this period, his tenancy will be deemed to have been extended for another 10 years.

These provisions of the Bombay Act have been followed in Hyderabad, Madhya Pradesh, Saurashtra and other States. The Punjab Tenants (Security of Tenure) Act of 1950 ensures security from ejectment for at least five years. The tenants of reserved land will have the right of re-instatement if, after their ejection, the landlord fails to cultivate land personally.

These Tenancy Acts have also sought to reduce the burden of rents. In Bombay, the maximum rent that can be recovered from a tenant has been fixed at one-fourth of the total produce in the case of irrigated lands and one-third in the case of other lands. The government have powers to lower these limits for any area. In Orissa, the Tenant's Protection Act of 1948 fixes the maximum rents of occupancy tenants at 1/6th to 1/3rd of the gross produce or value thereof. In Madras, the level of rents paid in Zemindari areas have been brought down to the level prevailing in other areas. Under the Andhra Tenancy Act of 1956, the rent to be paid by a cultivating tenant is not to exceed 45 p.c. of the gross produce in the case of commercial crops, and 28 p.c. to 50 p.c. in the case of other crops. Subject to this provision the actual rent is to be fixed either by agreement or by the Tehsildar.

Thus under the recent Acts, tenants enjoy the following rights, *viz.*, reasonable security of tenure, payment of fair rents, right to buy their holdings at reasonable prices determined by tribunals (as in Bombay or Andhra), or as on payment of a certain multiple of rent or land revenue (as in Punjab or U.P.).

As regards crop-sharing tenants, the Assam *Adhiars'* Protection and Regulation Act of 1949 has sought to grant occupancy rights on the *adhiar* unless he gives up the land or is asked by the Revenue

Officer to do so on certain definite grounds. The landlord will get back seed grains if he supplied them and also one-third of the produce if he has supplied plough and cattle. In other cases, he will get only one-fourth of the produce. In West Bengal, the Government have set up Conciliation Boards to settle disputes between the *bargadars* and owners over rent, ejection, supply of seeds etc. In the absence of any agreement, the seed will be taken out of the produce and given to the party that supplied it. The landlord and the tenant will each get one-third of the total produce. The remaining one-third will be divided between the parties in proportion to their respective contributions towards the costs of cultivation by way of supply of mancres, ploughs and cattle etc. In Andhra and Bombay, the Government have got the power to commute crop-rents into cash-rents.

Effects of land reforms

The net result of these land reform measures has been that most of the actual cultivators in the previous zemindari areas have obtained proprietory rights in land. Thus all occupancy ryots, ryots at fixed rates of rent etc. have become owners of land they hold. The non-occupancy ryots and under-ryots can become owners after paying a prescribed price. All of them, as also the original intermediaries who have been allowed to own their *sir* and *khud kast* lands, have now become the tenants of the State. It should, however, be noted that the position of tenants in the ryotwari areas is inferior to that of the tenants of the State in other areas.

Thus there are now more landowners in India than before the inauguration of the land reforms. But though proprietory rights over land have been conferred on a larger number of cultivating tenants, these laws have placed a number of restrictions on such rights. These restrictions generally relate to the right to sell, transfer, mortgage or lease land. Most States prohibit the sale of land to a non-agricul-turist. In Bombay and West Bengal, tenants in actual possession of land and the neighbouring cultivators and others have been given the right of pre-emption over the land proposed to be sold to third persons. With regard to backward class cultivators, some States have put restric-tions confining the sale of land only to persons belonging to the same group or area. Secondly, in U.P., though the *bhumidars* are allowed

to sell their holdings, there is a restriction that such a sale should not increase the buyer's holding to more than 30 acres. The corresponding restriction is 12 to 48 acres in Bombay, 50 acres in Madhya Pradesh, 25 acres in W. Bengal, 150 bighas for a family in Assam and 3 times the family holding in Hyderabad (Andhra). There is also a bar on the sale of land which would result in reducing the size of land remaining with the seller below the fixed floor. Thus in Bombay, Andhra and Madhya Pradesh, no sale of land is permitted which reduces the seller's holding below the prescribed limit. Similarly, laws in some States prohibit the mortgage of land with conditional sale except in the case of co-operatives. In most States, usufractuary mortgages are allowed only for a specified period. Lastly, in most of the States, the landholders are allowed to lease out their land, except in certain cases. Thus restrictions have been placed on the letting of land by new owners and sub-letting by tenants so that the area under tenancy is not greatly extended. Thus in M.P., the *pucca* tenants, who possess the right to sell land, have not, however, been given the right to sub-let their holdings except in specified cases. In W. Bengal, the ryots cannot sublet their land, except to the *bargadar*, though they possess the right to sell land. These restrictions are particularly stringent in the case of landholders belonging to the aboriginal tribes or backward classes.

Ceilings on land holdings

An important feature of the present land reforms is the fixation of ceilings on the holding of land by individual cultivators. The idea behind this policy is that no cultivator is to be allowed to hold more than a specified amount of land. Those persons whose present holdings are above this amount will be required to surrender the surplus land to the State, and this land is to be distributed among other persons in the following order of priority, *viz.*, (i) tenants displaced as a result of resumption of land for personal cultivation, (ii) farmers with uneconomic holdings, and (iii) landless workers. The Second Plan recommended that "the ceilings should be fixed at three times the family holding for an average family" of five in number. Where the number of members is larger, the ceiling may extend to a maximum of six family holdings. A large number of States have already passed legislation for fixing ceilings on land. Ceilings have been fixed at 40 acres of land in U.P., and Delhi, at 25 acres in W. Bengal, at 32 acres

in M.P., 30 (class I) to 90 (class II) acres in Bihar, 33 to 99 acres in Orissa, 30 acres in Rajasthan, 15 acres in Kerala. In some States, ceilings have been fixed in terms of income. Thus it is a land yielding a net income of Rs. 5400 in Andhra, Rs. 4200 in Mysore, Rs. 3600 in M.P. and Bombay. Those who hold land above these ceilings will have to surrender the surplus land to the State which would of course pay them suitable compensation.

The main justification for this policy lies in the desirability of the redistribution of land among landless labourers. In view of the existence of a large number of landless workers in the villages, it is essential to break up such large estates and to re-distribute the land above the ceilings among such persons. The result would be a stable village economy with a good deal of improvement in the economic position of a large number of unfortunate people. If it is undesirable to have large inequalities of income and property, it is equally undesirable to have a society in which some have land in excess of their requirements while others lack land.

There is, however, a large section of opinion which is highly critical of this proposal. In their opinion, the fixation of ceilings on land holdings would not bring much benefit to the people of even to the landless workers, while it would give rise to problems which, in their magnitude and intricacy, would more than counterbalance the gain if any. In the first place, it is doubtful whether, by fixation of ceilings on land, much land would be available for redistribution. And the surplus land would be available would be so scattered in patches all over the States. Secondly, the States would have to pay compensation to those landholders who would have to surrender their excess land. Since these landholders are not intermediaries but actual cultivators, the amount of compensation would have to be calculated on a just basis, and this would be a very complex and formidable affair. The State governments, in their present financial position, would not be able to make the necessary payments. Thirdly, the fixation of a ceiling in terms of acreage will involve a continual revision of the ceiling according to the rise or fall in agricultural prices. Such a ceiling will have no meaning unless it is fixed in terms of income. It must be such as to guarantee a given level of income to the landholders. Hence such ceilings should have to be calculated afresh with significant shifts in agricultural prices or yields. Moreover, this raises the important

question of the justification of fixing a ceiling on the incomes of the landholders when no such limit has been with regard to the incomes of other groups of persons. If land is scarce, so also are other assets. Hence justice demands that the fixation of a ceiling on landholding should be accompanied by similar limits on the ownership of other income-yielding assets.

Such a policy would seriously interfere with agricultural efficiency. Large holdings combine the benefits of large-scale cultivation and the working zeal of private ownership. Such holdings have everywhere been the receptacles of all that is progressive in agriculture. Moreover, if a comparatively low ceiling is fixed, the more enterprising among the cultivators, finding all avenues to betterment thus closed, would migrate to towns. This would deprive the rural sector of its most progressive element on whom the prospects of agricultural and other advancement in villages depend. Thus this policy would distort production and stand in the way of achieving significant increases in agricultural productivity.

Another serious criticism is that the fixation of ceilings would reduce the marketable surplus of foodgrains. The major portion of foodgrains offered for sale in the markets generally comes from the large landholders. But the idea behind the fixation of ceilings is to create a large number of very small holdings by breaking up large farms. All of the new allottees of the redistributed holdings may not be efficient cultivators. So production on the large farms which will be required to surrender land is likely to react adversely, and the output on the new small farms may not increase simultaneously. The small cultivators have generally little surplus to sell in the markets ; the produce on their small farms being required mostly for family consumption. As a result, both output and the marketable surplus of foodgrains may decline, at least in the earlier years, thereby increasing the difficulties of the food problem.

The proposed scheme of the distribution of the surplus land also raises certain very intricate issues. If the surplus land is to be distributed among the landless labourers, it would increase the number of uneconomic holdings as well as the pressure on land. Whatever benefits may thus accrue to the landless workers, these will be offset largely by the diminished employment opportunities for these workers

as a result of the break-up of the large holdings. The real land problem of this country is not thus one of distribution of "surplus" land, but of drawing the surplus labour away from land to other more remunerative occupations.

Questions

1. What are the factors which should govern the formulation of land tenure policy ? (Bom. 1953).

2. Write short notes on the problem of land reforms in India.

3 Examine the proposals for land reform suggested in the Five Year Plans. How far have they been carried out so far ? (Pat. 1958).

4 Give the trend of recent tenancy legislation passed in the States with the possible consequences on the agricultural economy. (All. 1944 ; Osm. 1958 ; Ag. 1953 ; Cal. 1941 ! Punj. 1957 ; J. K. 1958).

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* For a discussion of the Nagpur Proposals of land reform by the Congress, see Chapter 19.

CO-OPERATIVE MOVEMENT

Meaning of co-operation : In a broad sense co-operation means the mutual assistance of a number of people or of agents for performing a particular task. In this narrow sense it is used to describe a form of business organisation which is not carried on for the purpose of earning profits, but which is actuated by the spirit of mutual service. In a competitive economy, producers are influenced mainly by the profit motive. Their ideal is to earn the maximum profits for themselves. In a co-operative society, the members follow some other ideal. Such a society is generally formed by people who are poor for the purpose of promoting their common material and moral advantage. Individually each member may be unable to achieve some end by his own efforts. So he combines with others to secure this common economic end. The association is entirely on a voluntary basis, and each member possesses equal rights and responsibilities in the society.

A co-operative society may be formed for a variety of purposes. It may be formed by ordinary consumers for the purposes of conducting retail trade. This is known as the consumer's co-operative society or stores. It may also be formed for the purpose of producing a particular commodity or commodities. This is producers' co-operation. Thirdly, a co-operative society may be organised for the wholesale purchase of raw materials or instruments of production required by the members ; or for the bulk sale of commodities produced by the members. Lastly, a co-operative society may be formed for the purpose of raising funds and lending to the members, engaged in agriculture, industry or salaried occupations. This is the last form which predominates in India.

History of the movement in India : The history of the movement can be traced back to the last quarter of the 19th century when a number of co-operative credit societies was started in Punjab and U.P. for the purpose of granting loans to cultivators. The movement was looked upon as providing a means for the solution of the problem of rural indebtendness. At about this time the Madras government sent one of their officials, Sir Frederick Nicholson, to study the movement in Germany. Nicholson submitted his report in 1895-97, in

which he advocated the establishment of co-operative societies on the Raiffeisen model. The Famine Commission of 1901 also pointed to the need for organising such societies in the rural areas. Accordingly, the Government of India set up a committee in 1901 to report on the establishment of co-operative societies in India, and finally the Co-operative Credit Societies Act was passed in 1904. This Act laid the foundation of the co-operative movement in India.

The Co-operative Credit Societies Act provided only for the formation of credit societies for the grant of loans. These societies were divided into two types, rural and urban. Rural credit societies were to be organised on the Raiffeisen model. The liability of each member was to be unlimited ; there was to be no share capital ; and loans were to be granted only to members and only for productive purposes. Urban credit societies were to be organised on the Schulze-Delitsch model. They were to issue shares and the liability of the members was to be limited.

A large number of co-operative credit societies were started after the Act and the number of societies increased to about 10,000 by the end of the year, 1912. But a number of difficulties were found as a result of the working of the Act. It was considered necessary to start non-credit societies, which was not possible under the Act. Even with regard to credit societies, there were certain defects. The division of societies into rural and urban types was found to be unscientific. Moreover, there was no provision in the Act for the establishment of central societies for supervising the work of primary societies and for supplying funds to them. Lastly, more liberal provisions were found necessary for the payment of dividend.

To remedy these difficulties, another Act, the Co-operative Societies Act, was passed in 1912. It provided for the establishment of non-credit co-operative societies such as sale societies, purchase societies, housing societies etc. Secondly, it laid down the organisation of central societies like supervising and guaranteeing unions, central and State co-operative banks. Thirdly, it abolished the distinction between rural and urban societies, and introduced a new classification between societies with unlimited and limited liabilities. Societies formed mainly by agriculturists for the grant of credit were to have unlimited

liability, and the rest would have the option to choose between the two types.

After this Act, the movement began to spread out into many directions, and in 1914, the government appointed a committee, known as the Maclagan Committee, to review the progress achieved by the movement. The Committee made a number of useful recommendations to increase the efficiency of the movement. Under the Government of India Act of 1919, co-operation became a Provincial subject, and was transferred to the control of ministers. Many of the Provinces passed separate Acts to guide the movement in their respective areas, and the number of societies increased from 57·7 thousand in 1921-25 to 116·9 thousand in 1936-40. But the movement passed through considerable difficulties during the Great Depression of the thirties. On account of the serious fall in prices, most of the borrowers became unable to repay their loans on due dates. As a result, overdues became excessive in many societies. The World War II, however, led to some improvement by raising prices. Overdues decreased, and the working capital of the societies increased from Rs. 94·6 crores in 1931-35 to Rs. 188·7 crores in 1946-50.

Present position of the movement : The present position of the movement will be obvious from the statistics regarding the number and capital of the societies. In June 1964 there were more than 3 lakh co-operative societies with a membership of more than 15 crores and a total working capital of Rs. 381·70 crores. The vast majority of these societies are, of course, credit societies (about 68 p.c.); and about 90 p.c. of the credit societies are agricultural societies. Thus in spite of the spread of non-credit co-operation, credit societies are dominant in the movement. It may roughly be estimated that 21 p.c. of the population had been brought into the co-operative movement.

Apart from this general expansion, the movement has spread into several walks of life, which were perhaps no more than touched before. It is now playing an important part in the rehabilitation of displaced persons and in the Grow-More-Food campaigns. Through the organisation of housing, industrial and farming societies, a number of displaced persons have been settled in colonies and provided with gainful employment. Co-operative societies played an important role in the Grow-More-Food campaign. They are being entrusted by the govern-

ment with the distribution of manures, chemical fertilisers and agricultural implements. Another notable achievement has been the establishment of a large number of multi-purpose societies, notably in the States of Madras, Maharashtra and Uttar Pradesh.

At the end of June, 1964, there were more than 3 lakh societies of which 2·34 lakhs were credit institutions. The number of primary agricultural credit societies was 2·08 lakhs with 262 lakh members. These primary agricultural credit societies were looked after by 380 central co-operative banks, which were, in their turn, financed by 21 State Co-operative banks. In addition, there were 481 land mortgage banks of which 18 were central land mortgage banks. The non-agricultural credit societies numbered about 12 thousand of which about 50 p.c. were from the 4 States of Maharashtra, Mysore, Punjab and U. P. The non-credit societies, agricultural and non-agricultural, numbered about 1,12,112 in 1962-63.

State-wise distribution : An unfortunate feature of the movement is its uneven development. For instance, out of a total of 1,66,543 primary agricultural credit societies, 45·4 p.c. are concentrated in the 3 States Maharashtra, Madras and U.P. In Madras and Maharashtra the movement is well-developed. In 1962-63, rural credit societies covered 58·3 p.c. of the villages in the States. Moreover, out of a total number of 536 primary land mortgage banks, as many as 369 or 69 p.c. were concentrated in Andhra Pradesh, Madras and Mysore. On the non-credit side also, Madras and Maharashtra have made commendable progress in many spheres such as consumers stores, housing, milk supply, weavers' co-operative societies etc.

As regards other States, U.P., Madhya Pradesh, Bihar, Orissa, Mysore, Kerala and Andhra, the movement has made some progress in various spheres, specially after World War II. But the movement is not so strong or wide-spread as in Madras and Maharashtra.

The two States of Punjab and West Bengal stand in a separate category. Before the partition, Punjab had a fairly developed co-operative structure. But the partition of these States disrupted this structure. In undivided Bengal, the co-operative movement, though wide-spread, was very badly affected by the depression of the thirties, and the position became more difficult as large funds of the provincial

co-operative bank became frozen in East Bengal. In Assam also, the movement was hit hard by the depression from which it had not been able to emerge. So at present there is moribund credit structure in that State.

Structure of the co-operative movement : The base of the movement consists of the primary co-operative societies. These are to be divided into two groups, agricultural and non-agricultural, depending on the class of people who constitute these societies. Each of two types of societies can further be classified into credit and non-credit societies. So we have four different types of primary societies, *e.g.*, agricultural credit societies, agricultural non-credit societies, non-agricultural credit societies and non-agricultural non-credit societies. To supervise the working of these societies, there are unions of co-operative societies, formed by groups of primary societies.

To finance these primary societies, a large number of central co-operative banks have been established mainly at the district or taluka headquarters. At the head of these central banks stand the State Co-operative Bank whose main business is to meet the financial needs of the central banks.

Agricultural co-operative credit societies : Certain principles are followed in the organisation of these societies. These societies are highly democratic in organisation, and the members are expected to know each other intimately. As far as possible, members render honorary services to the society and transactions are generally confined to members. This type of society can be formed by ten or more persons who reside in a village or part of a village. The liability of the members is unlimited. The members form the General Committee of the society and elect a Managing Committee from among themselves. The Managing Committee is the executive organisation of the Society, and conducts its day-to-day affairs, subject to the approval of the General Committee. The General Committee may also appoint a paid Secretary for the efficient conduct of its business.

The working capital of the society is derived from (*a*) the entrance fees paid by the members at the time of admission, (*b*) the share capital subscribed by the members, (*c*) deposits from members and non-members, and (*d*) loans and deposits from other societies, central

co-operative banks and the government. Out of these funds, loans are granted only to the members for such productive purposes like current agricultural expenses, as for the purchase of seeds, implement and making permanent improvements to land. Loans are also given to enable members to meet such unproductive expenditure like marriage or sradh expenses, repayment of old debts etc. Loans are usually given against the personal security of the borrowers and also against the security of their property. These loans are to be repaid in easy instalments.

Every society is required to build up a reserve fund. In societies with no share capital, all profits are taken to the reserve fund. In societies with share capital, at least 25 p.c. of the profits are to be taken to the reserve fund before any dividend can be declared. The society may spend 10 p.c. of its profits for charitable purposes, subject to the sanction of the Registrar. The accounts of every society are audited by officers appointed by the Registrar. The societies have been granted certain special privileges like exemption from stamp duty, registration fees or income tax. They enjoy a prior claim over other creditors with the exception of the government.

These societies form the backbone of the whole movement. About 79 p.c. of the total number of agricultural co-operative societies consist of credit societies. Their number amounted to 2·08 lakhs with a working capital of Rs. 273·70 crores and a membership of 267 lakhs and deposits of Rs. 14·59 crores at the end of June, 1964.

Agricultural non-credit societies : These societies have been organised in various directions. There are co-operative purchase and sale societies, co-operative production and sale societies, co-operative irrigation societies, cattle insurance societies, co-operative consolidation of holdings societies, co-operative farming societies, co-operative better living societies etc. The organisation of these societies is similar to that of the credit societies, except that their liability is limited.

The most important group among non-credit societies is constituted by the co-operative marketing societies. These have been organised mainly for the sale of a single commodity produced by the members, such as the cotton sale societies of Maharashtra, sugarcane sale societies in Bihar and U.P. and Maharashtra, sugarcane sale societies in Maharashtra. An account of the working of these societies has already

been given in a former chapter. The number of primary agricultural non-credit societies stood at the end of 1962-63 at 32,155 with a membership of 1,24,27,000 and a working capital of Rs. 384·19 crores.

Non-agricultural credit societies : These are organised on the Schulze-Delitsch model with limited liability and share capital. These have been established to cater to the needs of various classes of people. The most prominent among them are the *urban banks* which number 916 with a working capital of Rs. 52·0 crores in 1963. These banks follow modern methods of banking and accept deposits from the public. These banks have made good progress in the States of Maharashtra, Madras, Mysore, West Bengal and Andhra. There are also *Salary-earners' societies,* formed to meet the needs of the middle class population who are gainfully employed. The progress made by these societies is quite satisfactory. There are certain factors in their favour. These are generally managed by educated people with assured incomes. Loans advanced are generally within the repaying capacity of the borrowers to whose income they bear a ratio which is within a particular maximum limit. Repayments are also regular and in many cases employers co-operate with the societies by effecting deductions from the monthly pay-rolls of the indebted employers. *Wage-earners' societies* such as mill-hands' societies are comparatively few in number and they are concentrated mainly in Maharashtra. In addition, there are other types of non-agricultural credit societies, such as *fishermen's* and others catering for the credit needs of persons of small means such as street hawkers, motor and ghari drivers, skilled workers like carpenters etc. One important feature of these societies is that a large number of them perform non-credit activities like the purchase and distribution of controlled and rationed articles, running fair price shops and retail shops, joint purchase and distribution of the domestic requirements of members etc.

Non-agricultural non-credit societies : There are various types of these societies, such as co-operative consumers' stores, co-operative housing societies, co-operative production societies, etc.

(1) *Consumers' co-operatives stores* are organised for the purchase and retail sale of the consumers' goods among the members. Members purchase shares in the society and are expected to buy all their requirements of consumer's goods from the stores. These goods are sold at

the current retail prices and at the end of the year each member receives a dividend depending on the total value of his purchases from the stores. These types of societies occupy a prominent position in the co-operative movement in Great Britain. But they are not important in India. There were in all 8,401 consumers' store in India with a membership of 16,06,426 members at the end of June, 1963. Moreover, except in Madras and to some extent Maharashtra and Assam, the movement has not spread to include the wholesale trade.

This movement has achieved some progress in Madras, where it has spread even into rural areas. This State has also organised a number of wholesale stores, whose financial position is generally sound. A special mention should be made of the progress and working of the school and college students' stores, whose number stood at 345 with a membership of 21186 students, 6203 teachers and a paid-up share capital of Rs. 81,618. In other States, the consumers' store movement gained some impetus since the World War II as the various governments encouraged their formation with a view to securing a better distribution of the controlled and rationed articles. It should be noted that besides the purely consumers' stores, numerous societies of other types, particularly credit and multi-purpose societies, have also undertaken the functions of the distribution of consumer's goods. Thus controls largely influenced the success of the stores movement in all States, and most of them are facing difficulties with the removal of controls.

(2) *Co-operative housing societies* : The years after the Second World War have witnessed considerable development of co-operative housing societies, though there were a few such societies working in some of the States. In recent years housing accommodation has become very scarce particularly in the big cities and building construction was very much restricted on account of the abnormal rise in building costs. Under such conditions, co-operative housing offers several advantages especially for the poorer sections of the population. The organisation of these societies is proceeding at a rapid pace in several States. For instance, in Madras, the number of such societies increased from 112 in 1939-40 to 740 in 1962-63. In Bombay, the number has similarly shot up from 99 to during 1940-1950. In West Bengal and Mysore. their number has increased from 49 and 37 to 141 and 506 during the years 1948 and 1963. In Madras, these societies constructed 2308 houses in 1962-63, the number increasing from 79 houses in 1947-48

to this figure. Similarly, in Bombay, the number of buildings constructed have increased from 158 in 1947-48 to 329 in 1949-50. The main difficulty faced by these societies is the lack of adequate finance. Governments in several States help these societies by the grant of loans.

(3) *Producers' co-operation* : The potentialities of the movement in the form of producers' societies are well-known. These can be of special help to the cottage and small-scale industries. A large number of such societies have been organised in the hand-loom industry. Madras has the largest number of weavers' societies (1125 societies with 2,32,209 members 2,28,263 looms), followed by West Bengal (973 societies with 69,355 members). U.P. has 1585 societies and Maharashtra 354 societies. Madras has organised an apex organisation, the Madras Handloom Weavers' Provincial Co-operative Society, with a working capital of Rs. 204·28 lakhs. This society distributes yarn to the primary societies and undertakes the marketing of cloth, and itself owns six collective weaving centres, five hand-loom factories, one printing factory and seven dye factories.

Similar societies have also been organised for other small-scale industries. In Maharashtra, the 538 such societies with a total working capital and sales of Rs. 67·05 lakhs and Rs. 57·92 lakhs respectively. These societies have been organised among tanning and leather workers, forest labourers and oil-men, rope-makers and bamboo workers. In Madras, such societies have been organised among metal workers, leather workers, potters and rope-makers.

The organisation of this type of society is expected to help the rehabilitation of small-scale industries on modern lines. Given adequate financial help, staff for management and training implements these will enable us to utilise the age-long skill of our artisans.

(4) *Other forms of non-credit co-operation* : In addition to the societies described above, co-operation has been employed in improving the living conditions of agricultural and industrial labour through the formation of labour contract societies, forest labourers' societies, transport societies and co-operative workshops. The chief aim of the labour contract societies is to secure employment for their members by taking up contracts for the construction and repair of roads, culverts, buildings etc. Besides these, women's co-operative have been organised

for promoting thrift and developing handicrafts and home industries particularly suited to their genius, such as hosiery, knitting, printing of cloth, production of ready-made garments, leather works etc. A few such societies run nursery schools as well as spinning and tailoring classes. There are also (*a*) better living societies whose main work include village sanitation, running of free schools etc., (*b*) medical aid and public health societies, some of which undertake management of dispensaries, selling medicines to the poor free of charge or at concessional rates ; (*c*) educational societies, organised to help the spread of education mostly in Bombay. In recent years co-operation has also been called upon to play its part in rehabilitating displaced persons and ex-servicemen.

(5) *Co-operative insurance* : These societies undertake all kinds of general insurance on a co-operative basis. In Bombay, there were 5 life insurance societies, one fire and general insurance society and one motor insurance society in 1949-50. In West Bengal, there were 10 life insurance societies, whose total business in force amounted to Rs. 2·8 crores in 1949-50. Mention should be made of the Indian Postal and Co-operative Insurance Society Ltd., whose membership has been thrown open to all the employees of the Union and State Governments throughout India. Unfortunately adequate attention has not been given to the organisation of this type of societies. At the end of 1962-63, there were 12,131 non-agricultural non- societies with a working capital of Rs. 12·61 crores.

Higher financing and supervising agencies : So far we have discussed the functioning of the primary co-operative societies. A number of institution have also been set-up to supervise and finance these societies. These are Unions, Central Co-operative banks and State Co-operative banks.

(a) *Unions* : This type of society is formed by uniting a number of primary societies into one organisation. Membership is open only to primary societies, and the actual management is carried on by a committee representing the member-societies. There are guaranteeing unions whose main function is to guarantee the loans taken by member-societies from the central co-operative banks. Supervising unions undertake the supervision of the member-societies and so serve as a link between them and the central co-operative banks.

(b) *Central co-operative banks* : These banks have been organised mainly for the purpose of providing loans to the primary societies. As primary societies are fromed mostly by poor people, their financial resource are seldom adequate. Hence there was a need for setting up special institutions for the supply of funds to these societies. The central co-operative banks have been organised to meet this need. They may be formed exclusively by primary societies, or by both primary societies and ordinary individuals. The former type is known as the pure type, in which only co-operative societies can become members. The latter is called the mixed type. Most of the central banks are of the second type.

The main function of these banks is to grant loans to the primary co-operative societies. They also help the primary societies in other ways. A primary society may be temporarily in possession of surplus funds which it finds difficult to invest. It can deposit these funds with the central bank and earn some interest. The central bank lends these funds to other primary societies which may be in needs of funds. In this way central banks help in adjusting and balancing the surplus and deficiencies of working capital of the primary societies, and so secure the best utilisation of the funds. Central co-operative banks also perform all kinds of ordinary banking business like the acceptance of deposits from the public, remittance of funds, collection of bills, cheques, and hundis etc. In 1962-63 these banks received deposits amounting to Rs. 145·64 crores, the major portion of which came from private individuals, and these constituted nearly 41·1 p.c. of the total working capital of these banks. Some of them also grant advances to private individuals. In addition, a large number of these banks have undertaken non-credit activities of varying types. For example, in Madras, they finance co-operatives for the procurement and distribution of food-grains, fertilisers, iron and steel etc. Some of them are also engaged in the retail distribution of foodstuffs and other essential articles like sugar, cloth, kerosene oil, etc. In June 1963, there were in all 386 central co-operative banks.

The report of the Reserve Bank of India makes a number of suggestions for improving and strengthening the organisation of central co-operative banks. First, the share capital structure of these banks is weak, being only 7·1 p.c. of the total working capital. The reserve funds are also comparatively inadequate. These banks should, therefore, try to increase the amount of share capital and to strengthen the reserve

fund. They should carry at least one-third of the profits to the reserve fund until the latter equals the paid-up capital. Secondly, they should make an intensive effort to attract more deposits, especially in the rural areas. Thirdly, they should take steps to decrease their commercial banking activities, and to reduce the rates of interest on loans. Lastly, more attention should be paid to an exact assessment of bad and doubtful debts, and to the creation of adequate reserves against them.

(c) *State co-operative banks* : These are situated at the capital of the State, and have been organised to finance and co-odinate the operations of the central co-operative banks. Their organisation varies in different States. In some of them membership is open both to the co-operative societies and to private individuals. In others, these banks are of a pure type, membership being open only to co-operative institutions. Their function is to grant loans to the central banks, and where there are no central banks, to primary societies. Secondly, they also help in the adjustment and balancing of the surpluses and deficiencies of the central banks. A central bank having surplus funds deposit them with the State Co-operative Bank, which lends them to another central bank suffering from a shortage of funds. In addition, they perform all kinds of ordinary banking business like the acceptance of deposits, collection of bills etc. They have also borrowed from the State Governments, the Reserve Bank of India, the State Bank of India and other sources. The Reserve Bank has been playing an increasing role in providing loans to the co-operative movement through the State Co-operative Banks at comparatively low rates of interest.

The growth and development of these banks have not been uniform in different States. While there are State Co-operative Banks which are extremely sound financially, there are others which are financially weak and are in occasional need of assistance from the State Government. There are State banks which are big organisations, while there are others that are smaller than even some of the central co-operative banks. Some State Co-operative Banks work under a constitution designed mainly to allow them to function as semi-trading co-operatives, while some others have concentrated chiefly on commercial business. At the end of June, 1963, there were 21 State Co-operative Banks.

Co-operation and long-term credit : The co-operative principle has also been adopted in the organisation of institutions designed to

supply long-term loans to the agriculturists. A number of land mortgage banks have been organised on the co-operative basis, though the mixed typed predominates among such institutions. We have already discussed the working of land mortgage banks in another chapter. At the end of June, 1963, there were 671 primary land mortgage banks, and they advanced loans worth Rs. 19·19 crores only. The number of central land mortgage banks was only 19 granting loans of Rs. 67·89 crores.

The State and the Co-operative movement :* The State in India has played an important role in organising and developing the co-operative movement. In fact, the movement may truly be regarded as predominantly state-sponsored. The aid given by the various State Governments may be classified as follows :—(1) Organisation of the movement through the co-operative departments. The birth and working of all co-operative societies are supervised by the co-operative department in each State. (2) Financial grants to the societies. The State Governments grant subsidies to the societies for several purposes such as meeting of establishment charges including staff, purchasing of equipment, agricultural implements etc. Broadly speaking, subsidies are given in the early stages of the working of societies with a view to help them to establish themselves firmly. In Madras and Maharashtra, the governments have adopted a scheme of subsidies with the object of cheapening credit to cultivators. In addition, the State Governments grant loans to the state co-operative banks. (3) Another way in which governments have been helping the movement is through the provision of guarantees of the principal and interest payments on the debentures of land mortgage banks. (4) The governments have also granted certain special concessions and privileges, such as exemption from income tax, stamp duty, registration fees, free remittances facilities etc.

The State Governments exercise control over the working of the societies through the conduct of auditing and inspection and supervision. The audit of societies is carried on each year by a separate staff maintained by the co-operative department. Inspection and supervision of societies are also carried on by the staff of the co-operative department.

General picture of the co-operative movement : It is now possible to get a general picture about the organisation of the co-

* *The Reserve Bank of India and Co-operative Credit,* see p. 85-87.

operative movement in India. The base of the whole organisation is the primary society. Most of them are single-purpose societies, designed to meet particular needs of the people of small means. The vast majority of these societies have been set up to serve the agriculturists, and more than 70 p.c. of these are concerned with the grant of loans. There has been some development in regard to the organisation of consumers' co-operative stores, and producers' co-operation or industrial co-operatives. But the proportion of these societies is comparatively small.

To finance these primary societies, a chain of other institutions has been set up. There are central co-operative banks or banking unions, which grant loans to the primary societies and supervise their operations. These central banks have again been federated into the State Co-operative Bank, which is the apex of the whole movement. The State Co-operative Bank and the central banks attract funds from the money market and invest them in financing the needs of these societies. The State Co-operative Banks enjoy important borrowing facilities from the Reserve Bank of India, the State Bank of India and other institutions in the money market and thus provide a channel through which the resources of the money market flow to feed the movement.

There is no doubt that co-operative credit has made a remarkable advance in many directions. Between 1951 and 1963, the total deposits of the apex co-operative banks increased from Rs. 22 crores to Rs. 97·31 crores, and those of the central co-operative banks from Rs. 38 crores to Rs. 145·64 crores in the same period. The deposits of the co-operative societies which formed 6·3% of the total deposits of the Indian banking system in 1951 now form about 8·8 p.c. in 1963. The total advances granted by the co-operative banks formed only 7·8 p.c. of the aggregate advances of the Indian banking system ; whereas they rose to 18·6 p.c. in 1963. These facts show that the progress made by the co-operative banks has not so far been insignificant, and there is no doubt that this type of credit has come to occupy an important place in our agricultural economy.

Single vs. multi-purpose societies : Until a few years ago, co-operative societies were organised for a single purpose, *viz.*, to supply credit, or to market the produce, or to irrigate the land etc. Since 1937, the Reserve Bank of India has been vigorously advocating the need for

organising multi-purpose societies. That is, instead of organising different societies to serve different purposes (co-operative credit society for loans, a co-operative sale society for marketing, a co-operative purchase society for the purchase of essential materials etc.), a single society should be set up to deal with all the needs of the cultivators. Such a multi-purpose society will grant loans to the members, buy good seeds, manure and implements for them, sell their produce, help them to consolidate their holdings and to irrigate their land, and to introduce other better-living measures.

Many advantages have been claimed in favour of such a multi-purpose society as against a single-purpose society. In the first place, there is a dearth of properly qualified men in the villages for the efficient conduct of so many single societies. Secondly, efficiency of the movement will also suffer because of another factor. To take an example, it is being increasingly felt that unless the supply of credit is linked up with the marketing of produce, it will not be possible to have fully efficient credit society or a marketing society. Efficiency of the whole organisation is likely to increase when both these functions and many others are combined in one institution. Lastly, only a multi-purpose society will be able to look after all the needs of the cultivators. Such a society will take a comprehensive picture of the whole situation and adopt all measures necessary for the allround rehabilitation of rural life. Credit societies meet only one need of the cultivators, and that too partially. The agriculturist has still to depend on the village money-lender for supplying him with other necessaries of life, *viz.*, consumers' goods and numerous other services that he was in need of. As a result, the idea of effecting an economic regeneration of the cultivators has remained unfulfilled. Only a multi-purpose society can embrace the whole life of the agriculturist and raise it to a higher level.

Advocates of single-purpose societies have, on the other hand, argued that a multi-purpose society would prove to be a cumbrous organisation and its working may overstrain the ability of the average villager. Secondly, in single-purpose societies, the failure of one of them will not involve others in danger. But in a multi-purpose society, failure in one line of business may bring down the whole organisation. Lastly, a multi-purpose society would necessarily embrace a large area

for efficient operation. This may give rise to a difficulty. In a single-purpose society, organised in a small area, members have opportunity to know each other intimately, and this knowledge and trust will help in the generation of the co-operative spirit. Such a spirit may be lacking in a multi-purpose society with its large area of operation and large number of members, most of whom may know each other only imperfectly.

Thanks to the vigorous advocacy of the Reserve Bank of India, the multi-purpose idea has obtained a firm footing in the co-operative movement. U.P. leads with 22786 multi-purpose societies, followed by Maharashtra (2161 societies) and West Bengal with 1641 societies. In U.P. the State Government has adopted a Development Plan which envisages the organisation of development blocks comprising 12 to 15 villages, with a multi-purpose society in each village. Starting with the improvement in agricultural production, these societies are intended to cover every aspect of rural economic life.

A critical assessment of the movement : The co-operative movement has conferred great benefits upon the country. In the first place, it supplies quite a large amount of capital to the members at reasonable rates of interest. Moreover, the benefits of the movement cannot be judged only by looking to the amount of capital lent by the societies. Where the co-operative movement has been strongly established, the competition of the societies has forced the money-lenders to lower the rates of interest. It has been estimated that this fall in interest rates has resulted in a saving of about one crore of rupees. *Secondly*, the movement has made important contributions towards the development of banking facilities in the rural areas. The agricultural credit societies received deposits worth Rs. 20·32 crores in 1962-63, and the central and state banks collected Rs. 242·95 crores. Thus these societies have encouraged habits of saving and investment. *Thirdly*, these societies have helped considerably in discouraging borrowing for consumption purposes—as it is well-known that they prefer borrowing for productive purposes.

Fourthly, the movement has thus been of great advantage to the premier industry of the country and to some of the cottage industries. By popularising the use of better seeds, cheap manures, and better implements ; by consolidating scattered holdings into large plots ; by

enabling the cultivators to get higher prices for their produce through improved marketing, and in various other ways, the co-operative societies are playing an important part in the improvement of agriculture.

Finally, the benefits of the movement cannot be measured only in economic terms. The moral and social benefits are no less obvious. Where the co-operative movement is strong, there has taken place a reduction in litigation and extravagance, drunkenness and gambling. In their place will be found industry, self-reliance and straight-dealing, education and arbitration societies, thrift, self-help and mutual help. It has increased the desire for education among the illiterate villagers. A large number of societies are spending a part of their incomes for the maintenance of educational and charitable institutions.

In spite of the achievements of the movement, it has been subjected to serious criticisms. In first place, it has been urged that most of the benefits that are claimed on behalf of the movement are of non-economic nature, and these are difficult to measure. Moreover, these benefits become available only where there are good societies, and the number of such societies is not large.

Secondly, the vast majority of the societies have been organised for the supply of credit, and let us examine their achievements. The amount of fresh advances granted by the agricultural credit societies was only Rs. 257·37 crores. This forms only a very small part of the total requirements of the agriculturists. Hence it is no exaggeration to say that the movement has touched only the fringe of the problem.

Thirdly, a number of defects can be found in the working of many of these societies. According to audit classification, the bulk of the societies in most States belong to the C class. In West Bengal, Bihar and U.P., only 0·6, 2·6, and 0·6, per cent of the societies belong to the A and B class. Several official enquires have revealed that a large number of societies suffer from the following defects : (*a*) Loans have been often given on an indiscreet basis without proper enquiry. In many cases loans have repeatedly been granted to a few favourites of the managing committee. A number of loans are in reality *benami* transactions. (*b*) Borrowers are not always punctual in repayment, and in many cases the Managing Committees have shown an excessive tenderness in dealing with such defaulters. In many cases fictitious repayments are recorded and borrowers have been granted fresh loans

on the same dates. As a result, the proportion of overdue loans and bad debts is quite large. (*c*) Most of the members do not take any interest in the working of these societies.

Fourthly, though the main principle of the movement is to encourage thrift and self-help it has not succeeded in attracting a considerable volume of funds from the members. As a result, the societies and the co-operative banks had to depend increasingly on external sources for the supply of funds. This is a discouraging feature of the movement.

The most serious charge against the movement is that the fundamental principle of true co-operation is lacking. The fact of the matter is that the organisers of the movement have been too eager to rush the pace of development. They have looked more to extensive than to intensive development and tried to increase the number at the cost of quality. In villages with their illiterate population it is not an easy task to find men possessing the requisite ability and knowledge to run these societies on the true co-operative principle. The movement has also suffered on account of a lack of training on the part of the staff of the co-operative department.

The Recommendations of the Rural Credit Survey Committee : It is generally agreed that the co-operative banks provide the most important instrument for the supply of rural credit. In India, the co-operative movement is comparatively weak in many of the States. The rate of interest paid by the members of the co-operative credit societies seems to be high in some of the States. Hence there is an urgent need for a more balanced, strong and well-ordered development of the movement so that agriculturists would be able to obtain finance at reasonably cheap rates of interest. We are going to point out an outline of the broad pattern of reorganisation suggested in the Rural Credit Survey Committee.

The Committee came to the conclusion that the old formula regarding one society for one village has failed in this country. So it recommended that in future, all primary societies should be of much larger size, comprising a number of villages with a reasonably large membership and a reasonably adequate share capital. A phased programme for the re-organisation of existing societies on this basis should be drawn up. Each of these societies should have an initial

minimum level of share capital to be raised in a specified period to an optimum level. In the initial stage, the central co-operative banks should contribute to the share capital as might be necessary for ensuring that it is not below the minimum level. In order to enable the central banks to do this, the State Co-operative Banks should provide the necessary funds to them, and the State governments should, in their turn, provide adequate funds to the State Co-operative Banks. Every such society should have a paid, full-time qualified secretary. In regard to loan operations, the emphasis should be on crop loans. Apart from crop loans, the primary credit societies may provide medium-term loans for productive purposes. They may also supply the members' requirements for crop production such as seed, fertilizers, and agricultural implements. Where suitable, they may also supply basic consumers' goods (sugar, kerosene, matches etc.).

The system of co-operative credit should be integrated with co-operative marketing. The Committee recommended that primary marketing societies should be established at important mandis or at taluka centres. In the case of these societies, the government should make a direct contribution to the share capital, and provide trained personnel for performing various technical functions. There should be a close link between the primary credit societies and the marketing societies, and the former should agree to provide loans to the members on the condition that the produce is sold through the marketing societies.

With regard to the higher types of societies (such as central co-operative banks, State Co-operative Banks etc.) each State government should draw up a definite programme for the re-organisation of these institutions on the basis of great State partnership. At the apex level, *i.e.* in the case of the State Co-operative Banks, or State Marketing Societies etc., the State should be the major partner and should directly contribute to their share capital. At the district level (*i.e.* in the case of the central banks), the State partnership should be through the apex institution. It would provide the funds to enable the latter to contribute to the share capital of the central co-operative banks. In the case of the marketing and processing societies, the State government should directly contribute to their share capital. At the

apex and central levels invariably not less than 51 p.c. of the share capital should be contributed by the State government.

The other important change that has been suggested is for the co-operative societies to adopt the practice of granting loans to members not on the basis of their title to land, but on that of their production needs. Short-term loans are to be given on the security of the expected crop, and the loans are to be related in amount to the estimated outlay on raising the crop, and recoveries are to be made, as and when the crop is sold, from the proceeds of the sale.

The Committee have, therefore, drawn up a scheme of integrated co-operative development which, in effect, envisages re-organisation and strengthening of the credit structure with larger units covering wide but compact areas, adequate turnover, paid management, state partnership and linking credit with marketing. A programme of development on these lines has been drawn up and it has been decided to establish, within the next 4 years, 10,400 credit societies, 1300 marketing societies and to build a number of warehouses at various places throughout the country. Each State is also to set up a Central Land Mortgage Bank, and as soon as the relevent development at the primary and other stages has been made, it should also establish a State co-operative marketing society.

In addition to increased State participation, the Reserve Bank would also be required to play an increasingly active dole. It should set up a National Agricultural Credit (long-term operations) Fund and the National Agricultural Credit (stabilisation) Fund. The former Fund is to be utilised to grant long-term lons to the State governments for enabling them to subscribe to the share capital of the co-operative institutions. The second Fund is to be utilised for the purpose of granting medium-term loans to State Co-operative Banks etc. in circumstances in which it is satisfied that short-term loans granted to such Banks of which repayment is due cannot be repaid on account of famine, draught etc, Each State Co-operative Bank and the central co-operative banks, and wherever possible, the larger sized primary credit societies should also institute individual Agricultural Stabilisation Funds of their own to enable them to carry over short-term loans due to them that cannot be repaid on account of famine, draught etc.

The Committee was fully aware of the point that increased State participation went against the fundamental co-operative principle. So it recommended that, after the share capital of each society had reached the optimum level fixed for it, steps should be taken to retire the shares of the government gradually out of the contributions of the members.

There is no doubt that the recommendations of the Committee cut across some of the vital principles of the co-operative movement such as increased State participation, larger size of the societies, paid service, etc. The linking of credit with marketing is a step in the right direction, so also is the insistence on the making of adequate provisions for the training of the personnel which is to run these societies. Time alone will show whether increased State participation and larger sizes would help, instead of hindering, the task of creating an appropriate "climate in which the small man who has so far had little opportunity of participating in the immense possibilities of growth is enabled to put in his best in the interest of a higher standard of life for himself and increased prosperity for the country."

Some current problems: The co-operative movement is now face to face with a number of special problems of its own. Two of them follow from the recommendations of the Rural Credit Survey Committee. One is the question of the size and nature of the co-operative societies and the extent of State help. The second is the nature of securities to be kept for the loans. These will be discussed below. The other problem relates to the formation of co-operative farming societies to solve the difficulties created by the existence of the innumerable small agricultural holdings. This has already been discussed in a previous chapter.

Large societies vs. one-village societies: The Rural Credit Survey Committee recommended the formation of large-size societies as against the small societies which had existed so long. The small societies had, in their opinion, proved unsuccessful in most cases. If co-operation was to succeed, the granting of loans should be combined with marketing and the provision of other services in one society as far as possible. The conduct of the business of the co-operative societies has now become a skilled and complicated one, and it would be necessary to entrust this to men specially trained for this purpose. In other

words, the societies must engage the services of a trained secretary and staff for the efficient conduct of their business. Only a large society can afford to employ such a staff. A small society would not have enough income to pay for the services of trained men. Hence the committee recommended the formation of large-size societies. In order that such societies would have enough resources from the beginning, the State should be asked to subscribe to the share capital of these societies.

Both these points have been seriously questioned by a large group of co-operators including Sir Malcolm Darling. They argue that the large-size co-operatives would tend to be unwieldly. One of the fundamental principles of co-operation is that members should know one another intimately. But this would be impossible in a large society. In some States like U.P. there are large societies covering as many as 25 to 50 villages. Such societies have virtually ceased to be a co-operative institution. They will be unable to maintain contact with all members and to estimate the credit needs of a vast membership. As a result, members belonging to villages where the headquarters of the large-size co-operatives are likely to receive more attention than the rest.

Another group of objections relate to the question of State participation as proposed in the Report. It is argued that the participation of the State government in the share capital and the management of the societies goes counter to the basic principles of co-operation. Co-operation is a movement that should spring from the people and be run wholly by the people. The domination by the government would undermine such qualities as self-help, thrift etc. among the members.

The weight of these criticisms led to a subsequent change in opinion, and the National Development Council have recently given their verdict in favour of the principle, one village, one society. As a result, work on the conversion of small societies into large size co-operatives has been stopped.

The question of the size of co-operative societies has been examined by the Vaikunth N. Mehta Committee on Co-operative Credit, which has issued its report in June 1960. In the Committee's view, the size of a co-operative society should be determined by economic viability alone, and not by any other considerations. It is not desirable to have too large a membership and too extensive an area for a society. The

majority are of the view that the population covered by a society should not exceed 3,000 or about 600 families.

Regarding State participation, the Mehta Committee have supported such a measure subject to certain conditions. The State should participate in the share capital of viable primary credit societies through apex and central banks. Such contribution should range between Rs. 1000 and Rs. 10,000 provided that it does not exceed the contributions of members. The minimum contribution should be paid only when a society collects additional share capital of Rs. 3,000 from its numbers over a period of 3 to 5 years. The State contribution should be repaid after a certain period. The Committee have also recommended the grant of a subsidy of Rs. 1200 to each society by the government for 5 years.

The changing character of the co-operative societies will be evident from the fact that while in 1956-57, the number of large size societies was 162,000 as against about 1600,000 small societies. But by June 1961, the number of the former had fallen to 79,000, while that of the latter had increased to 2,042,000.

Another noticeable change has been with respect to unlimited liability. In 1950-51, out of a total of 1.05 lakh societies, 0.758 lakh societies were organised on the unlimited liability basis. But by June, 1961, their number had dwindled to only 0.854 lakhs out of a total of 2.12 lakh societies. They now form only 40 p.c. of the total number of agricultural credit societies as against 72 p.c. in 1950-51.

The problem of crop loans : Another innovation suggested in the Report was that the societies should in future grant loans not against the security of land, but on the basis of an estimate of the future buying capacities of the borrowers. The existing practice is for the societies to grant loans to the members against the security of land. As most of the members possess only very small holdings they can only be given small sums as loans which are clearly inadequate. As against this practice, it has been stated that the proper security against a loan should be the future paying capacity of the borrower. A cultivator may have a small plot of land. But if he is given loans to enable him to raise the output from land several times, he will be able to repay the loan quite easily out of the sale proceeds of the crops. In other words, loans are to be granted on the basis, not of the value of land given as security, but of the value of the crops likely to be grown on the land.

While this is a desirable reform, great caution is necessary for the grant of such types of loans. It is not an easy task to make a proper estimate of the likely increase in the amount of crops to be raised from a plot of land or of the value of the additional produce. The risks of over-estimation are likely to be large, and this may involve the societies in losses.

The Vaikunth Mehta Committee of 1960 have recommended in favour of the proposal. In their opinion, no cultivator should be denied credit facilities merely on the ground that he does not own land or cannot produce owners of land as sureties. Even cultivating tenant members should be provided loans according to the requirements of agricultural production on the basis of their repaying capacities and on adequate securities who need not necessarily be owners of land. But care should be taken to see that while credit should be adequate for production requirements, it should not be so facile or inadequately supervised as to render possible its use for consumption rather than increase in production. It recommended that in order to minimise the scope for misuse loans should be granted in the form of seeds, implements, fertilisers etc.

Service co-operatives : The Nagpur resolution of the Congress has laid down a programme for the development of service co-operative farms. These societies are expected not only to grant loans, but also to market the produce and to provide different services *e.g.* supply of good seeds, manure, implements etc. to the cultivators. These societies are to be formed on the basis of one society for one village, and the minimum membership should be 40 to 50 members with a minimum paid-up capital of Rs. 400 to Rs. 500. The government will give a subsidy of about Rs. 900 to each society for 5 years at the outset to enable it to employ a part-time trained manager. By the end of November 1959, 15,000 service co-operatives had been set up, and during the last year of the Second plan about 38,800 service co-operatives were set up.

According to the present policy, the emphasis is being placed on the promotion and development of "Service Co-operatives" with the primary functions of provision of short and medium-term loans, supply of agricultural requirements and the collection and sale of agricultural produce through the marketing society. In addition, these societies are to aid in formulating and implementing plans for increasing agricultural production.

Co-operative Credit and Banking Laws : As has already been pointed out, the Reserve Bank has been extending large amounts of credit to the State Co-operative Banks at concessional rates of interest. As the amount involved is getting larger with the passing of years, and as the activities of the State Co-operative Banks are expanding, the government passed the Banking Laws (Application to Co-operative Societies) Act in 1965 at the request of the Reserve Bank. The Act provides for the application of certain sections of the Reserve Bank of India Act of 1934 and of the Banking Act of 1949 to the State Co-operative Banks, Central Co-operative Banks and the more important primary non-agricultural credit societies, including in particular, urban co-operative banks with paid-up capital and reserves of Rs. 1 lakh and above. The State Co-operative Banks are now to be granted the full status of scheduled banks with its attendant privileges and obligations. Further, every co-operative bank, other than the State Co-operative Banks, has to maintain a cash reserve of not less than 3 p.c. of its total demand and time liabilities either with itself or in current account with the higher financing agencies. It has also to maintain liquid assets (including the 3 p.c. cash balances) of not less than 20 p.c. of its total demand and time liabilities for a period of 2 years. This is to be raised subsequently to 28 p.c. as in the case of other scheduled banks. The co-operative banks are prohibited from granting unsecured loans and advances to the Directors. The Reserve Bank may, however, allow the primary co-operative banks to grant such loans to their directors on such terms and conditions as may be approved by it. The Reserve Bank can also extend the provisions of the selective credit control to the operations of the banks under its powers to issue directives to all or any of them. All existing co-operative banks will have to take out a licence from the Reserve Bank. Co-operative societies other than co-operative banks, primary credit societies, and land mortgage banks will not be allowed to carry on banking business after a period of one year. Opening of branches by the State and the primary co-operative banks will require the approval of the Reserve Bank. The Reserve Bank has now been statutorily authorised to carry out inspections of these banks. The only difference is that the Reserve Bank has not been given the power to supersede, wind up, amalgamate or reconstruct these co-operative banks. These powers have been left with the Registrars of the Co-operative Societies.

Thus this act is designed to place the bigger co-operative banks almost on the same footing as the scheduled banks, giving them the same access to the Reserve Bank. This is likely to strengthen public confidence in these banks and so enable them to attract more deposits from the public. They will then be able to provide more funds to their members. Negotiations are being carried on to apply the Deposit Insurance Corporation Act to these banks as well so as to inspire more confidence in them. While this is a welcome feature, care should be taken to ensure that banks did not lose their entity as a part of the vast co-operative structure. While these banks committed the mistake of regarding themselves as co-operative institutions, neglecting their banking aspect, they should not now fall into the other error—that of behaving as commercial banks and neglecting their essentially co-operative character.

Questions

1. Trace the growth of the co-operative movement in India. (Cal. 1956; Nag. 1941; Punj. 1928; Osm. 1958; Luck. 1958; Mad. 1958).

2. Describe the main features and the different forms of Co-operative Societies in India. (All. 1942).

3. Describe the organisation and functions of the Primary Co-operative Credit Societies. (Ag. 1938).

4. Write notes on (*a*) Central Co-operative Banks and (*b*) State Co-operative Banks.

5. Account for the relative backwardness of the non-credit co-operative societies in India. Discuss their present position. (Punj. 1942).

6. How far has the co-operative movements succeeded in fulfilling the credit needs of Indian agriculture? What are its main drawbacks? (Jammu and Kash. 1953).

7. What are the various ways in which co-operation can solve the problems of (a) agricultural marketing, and (b) rural industries in India? (Gau. 1953; All. 1942).

8. Discuss the possibilities of co-operation in respect of (*a*) agriculture, and (*b*) cottage industries. (Cal. 1948, 1945).

9. What do you understand by a multi-purpose co-operative society? How far has this type been successful in India? (Del., 1953; Ag. 1953; Pat. 1953; All. 1941).

10. Examine in detail the actual and possible benefits of the co-operative movement in India. (Cal. 1953, 1949 ; Punj. 1933).

11. Account for the present unsatisfactory state of the co-operative movement. How can the position be improved ? (All. 1944 ; Cal. Hons. 1957 ; Punj. 1941).

12. Examine the role of co-operative movement in agricultural development. (Punjab 1959).

CHAPTER 19 THE FOOD PROBLEM

The Bengal famine of 1943 and the almost chronic food shortage from that year, the need for importing large quantities of foodgrains and the pressure of population have drawn everybody's attention to the "food problem" of our country. It is, therefore, necessary to examine the nature of this problem, and the relationship between our growing population and the almost stagnant food production.

The problem of food supply has three aspects. In the first place, there is the question of securing an adequate supply of the essential foodgrains to maintain the existing low level of consumption for a rapidly growing population. This is the purely quantitative aspect of the problem. Secondly, there is the problem of filling gaps in food consumption so as to bring the average diet to a physiologically adequate standard. This is the qualitative aspect of the problem. Lastly, there is the necessity for raising the average standard so as to enable everybody to enjoy a properly balanced diet, instead of the present miserable level of consumption. This is our ultimate goal. The problem has, therefore, immediate as well as long-term aspects. The immediate task is to satisfy the obvious hunger of the growing population by increasing the quantity of the basic foodgrains. We must seek to convert this 'deficit' into 'hand-mouth' economy. The long-term objective will be to provide an adequate and balance diet for all.

It should be noted that food shortage is not a recent phenomena. If we exclude Burma, India had been forced to import foodgrains from the end of the first world war. During the 5 years, 1920-25, India imported 0·16 m. tons of foodgrains, and the imports increased to 1·39 million tons during 1935-1940. The position was concealed upto 1937 on account of the inclusion of Burma, a surplus rice-producing country, in India. The fact that India was a food importing country became obvious after the separation of Burma. The position was, however, not serious on the eve of the second world war because the food deficit was comparatively small, and was easily made good through imports from Burma and other countries. The occupation of the south-east Asian countries by Japan stopped all these imports and this was an important cause of the Bengal famine of 1943.

Causes of food shortage : The present food situation is the outcome of several factors. One is of course the high rate of growth of population. As it has already been pointed out in the chapter on population that the population has been growing at a much faster rate since 1951 than during any other previous decade. This by itself increased the demand for foodgrains by large percentages. Secondly, there has taken place a considerable increase in the level of money incomes in the country as a result of the large investment expenditure under the 3 plans. As the vast majority of the people are very poor, the income elasticity of demand for food is very high. There is no doubt that as compared to any previous decade, money incomes have risen at higher rates, and this has caused the demand for foodgrains to rise by a very large percentage. Thus while population has been growing at a high rate, their demand for food has also been rising at an accelerated rate on account of the rising money incomes.

These two factors would not have mattered if the production of foodgrains could have been increased proportionately. Unfortunately in spite of the large investment in agriculture made during the 3 plan periods, the production of foodcrops could not be increased as planned for on account of a number of acts of God in the shape of floods, droughts and cyclones. Thus the total foodgrains production rose from 54·9 million tons in 1950-51 to only 72·3 million tons in 1965-66, *i.e.* by 31·7 p.c. over a period of 15 years. The growth of population itself has proceeded at a higher rate during this period. If, at the same time, the demand for food has been rising fast due to the high income elasticity of demand for food and increasing money incomes, there is no wonder that the country would be suffering from food shortage. The comparatively slow rate of advance in food production has been due to a number of factors, such as a series of bad monsoons, cyclonic weather etc. This has also been due to the failure to re-organise or re-galvanise the agricultural productive system.

The comparatively slow rate of increase in food production has been further aggravated by the decline or the still slower rates of growth in what has been called the marketable surplus. There is a dispute as to why this happaned. According to the Report of the Foodgrains Enquiry Committee, there are three reasons for this decline in the quantity of foodgrains offered for sale in the markets ;—the cultivators are consuming more food than before, they are selling less in the market

as they can meet their cash requirements by selling a smaller quantity at higher prices, and lastly there is more speculative hoarding of food-grains in anticipation of higher prices. The first two factors have been called in question. It is doubtful how far the cash needs of the cultivators are so fixed that once they get higher prices, they will sell a smaller quantity of the produce in the market and eat the rest at home. Why should they not meet their other pressing needs by selling the same amount of crops as before, or even by selling a little more with a rise in the yield of crops? Those who argue in that manner assume that the needs of the cultivators for everything else except food is more or less absolutely fixed. This is a doubtful hypothesis. There is however a good deal of force in the third argument, that large producers and dealers may be holding back stocks in expectation of higher prices. Government's price policies have also been unrealistic, and have often failed to take proper account of the actual market conditions. They have also lacked firmness and consistency. The result of all these factors has been the vary steep rise in the prices of foodgrains that had taken place during the third plan period.

The result has been a widening gap between food supply and population, a gap which had to be met partly by cutting down food consumption and partly by importing foodgrains. Imports of food-grains amounted to 2·84 million tons in 1948, 3·71 million tons in 1949, 2·12 million tons in 1950, 4·73 million tons in 1951 and 3·44 million tons in 1961. The imbalance between population and food supply can also be verified by the cultivated area in reference to land-man (*i.e.* land per head of population) relationship. In 1911-12 the total cultivated area per head of population was 0·88 acre. It is now only 0·74 acre per head and the net area under foodgrains is only 0·51 acre per head. It has been estimated that the minimum area required for producing food crops is at least 0·63 acre per head on the basis of the present levels of consumption and the standard of cultivation. So the deficit on account of land-man relationship comes to about 19 p.c.

Nature and extent of the shortage: What is the extent of deficit in our food supply? Recently the Ford Foundation Team of agricultural specialists have placed the total requirements for foodgrains at 110 million tons by the end of the Third Plan. They arrived at this figure by assuming that the population would number 480 milions by 1966, and the net daily per capita consumption of foodgrains would

amount to 18 oz. At the present rate of increase in foodgrains production, there would be a gap of 28 million tons between demand and supply. The rate of increase in the production of foodgrains for the next 7 years will have to be stepped up to 8·2 p.c. per year as compared with an annual average of 3·2 p.c. from 1952-53 to 1958-59.

But expectations regarding food production during the 3rd Plan period have not been fulfilled. Total foodgrains production which amounted to 82·0 million tons in 1960-61 increased to only 82·7 million tons in 1961-62, but declined in course of the next 2 years to 78·4 million tons in 1962-63. It recovered subsequently to 89·0 million tons in 1964-65. But it fell again to the very low level of 72·3 million tons in 1965-66. The production of rice fell from 36·9 million tons in 1963-64 to 30·6 million tons in 1965-66. The resultant imbalance between the supply and the demand brought about a very steep rise in the prices of foodgrains. The index number of food prices rose by 14·2 p.c. in 1963-64, by 8·9 p.c. in 1964-65 and by 14·3 p.c. in 1965-66. The rise in the case of the prices of rice was very steep, being by 23·9 p.c. in 1965-66 ; prices of edible oils rose by 43·5 p.c. This was due to the fact, among others, that market arrivals of rice in selected markets declined during 1965-66.

Studying the problem on a regional basis, only a few States (*viz.*, Assam, Madhya Pradesh, Orissa and Punjab) including about 28 p.c. of the area and 82 p.c. of the population are deficit in food production.

This is the extent of estimated food shortage from the quantitative point of view. If the aim is to provide a balanced diet for the average population, our deficiency in respect of the various kinds of food-stuffs has been estimated as follows :—

Table 22

ITEMS	QUANTITY (MILLION TONS)	PER CENT OF TOTAL PRODUCTION
Cereals	6	10
Pulses	1·5	20
Vegetables	9	100
Milk	70	300
Meat, Fish and Eggs	4·5	300
Fats and Oils	5·0	250
Fruits	3·0	50

Government Policies : The shortfall in food production with the consequent steep rise in food prices led to the adoption of a number of measures by the government. These measures fall into the following groups. To cope with the immediate problem of smaller availability of foodgrains, principally rice and wheat, the government proceeded by steps to adopt the following measures ;—introduction of rationing in a full or modified form to isolate the areas where the demand for foodgrains would be likely to remain high on account of the higher levels of money incomes prevailing in these areas. The system of modified rationing, *i.e.* supply of partial quantities of foodgrains at comparatively low prices, was also motivated by the desire to come to the aid of the extremely poor and otherwise helpless class of people. To enable the government to distribute foodgrains through the rationshops, a levy was imposed on certain groups of growers or on almost all growers and millowners, requiring them to sell a part or the whole of their surplus stocks of foodgrains to the government at controlled prices. A large number of fair price shops were also opened for the sale of foodgrains at controlled prices. To enable the government to collect sufficient stocks of foodgrains from the surplus areas, a system of zoning was introduced according to which the surplus areas or districts of States were to be cordoned off from the rest of the country, and the movement of grains from one zone or cordoned area to another was prohibited. Another measure was the large import of foodgrains into the country, especially from the USA under the PL 480.

The following measures were undertaken to check the speculative holding of stocks of foodgrains. The Reserve Bank adopted the policy of selective credit control and attempted to restrict the granting of bank loans for financing such hoarding of foodgrains. All traders and the large growers were obliged to take out licences and to declare their stocks of foodgrains, and any one found to be in possession of any excess quantity was to be severely dealt with under the law.

All these steps were re-inforced by the adoption of measures for increasing the production of foodgrains such as the construction of minor irrigation works, schemes for the better utilisation of water from the major irrigation projects, provision of manures and fertilisers to the land, distribution of high yielding seeds etc.

Most of these measures came to be adopted in course of the second and the third plans, especially during the latter period. Thus

statutory rationing was introduced in Greater Calcutta, Asansol, Durgapur, Siliguri, Delhi, Madras, Coimbatore, Visakhapatnam, Hyderabad, Kanpur, Bombay, Poona, Nagpur and Sholapur. The number of Fair Price Shops were increased to 1,10,283 at the end of 1965. The scope and intensity of the schemes for the procurement of foodgrains were intensified, and Assam, Orissa and Maharashtra introduced the scheme of the monopoly procurement of paddy from the cultivators. In other States, a levy was imposed on millers and traders and cultivators on the basis of the number of acres cultivated by them. In 1965, the government set up the Food Corporation of India with the primary object of undertaking purchase, storage, movement and distribution of foodgrains and other foodstuffs. The FCI has already undertaken the post-procurement operations of rice involving quality control, purchase, transportation, storage and issue of rice procured on central government account in Andhra Pradesh and Madras for supply to Kerala and other deficit States. Mention should also be made of the adoption of the policy of fixing support prices for cereals in order to provide an incentive to the growers. A programme for an Emergency Food Production Drive was also adopted including the introduction of additional crops in selected irrigated areas, promotion of the cultivation of subsidiary root crops like potatoes, and topioca, preparation of farm manure in compost pits on a well-planned basis and the quick establishment of additional capacity for the manufacture of fertilisers etc.

But it is well-known that these measures have not resulted in halting the rise in foodprices. That they have relieved distress in many areas, and succeeded in restraining the rise in prices cannot be doubted. Thus though the price of rice had risen to as high as Rs. 2·50 per kg. in black markets in many areas surrounding Greater Calcutta, there is no doubt that in the absence of statutory rationing in that region, which served to restrain the demand for rice on the part of the consumers in Greater Calcutta, prices of rice would have risen still higher. The most serious criticism lies with respect to the failure to secure the planned increase in food production.' In the face of such stagnation in the agricultural sector it is doubtful whether any other combination of policies would have yielded better results.

Food production and economic development : In the normal course of development the shortage in food production in India is likely to prove a great problem. The partition of the country, the almost

stagnant agricultural methods, the ever growing population, the extremely low yield of crops, all these combined in the forties to bring about a serious situation on the food front. The low standard of living of the vast majority of the population contained the germs of an acute food crisis. Even a small rise in the money incomes of such people would lead to a considerable rise in the demand for foodgrains, and herein lay the dilemma of a rapid rate of economic development. Since the fifties, the pace of development has been considerably quickened, and the level of money incomes has tended to rise at faster rates. This has affected the demand for foodgrains in two ways. As the majority of the people have a very low standard of living, a rise in their money incomes will induce them to spend a larger proportion of these money incomes on foodgrains. The result of a rapid rate of economic development has therefore meant a large increase in the demand for foodgrains. Secondly, insofar as economic development is followed by more and more urbanisation, the demand for foodgrains would also increase more than proportionately. Moreover, the growth in urbanisation adds to the problem in another way. When people leave the villages and move over to the towns, it becomes necessary to import more food into the urban markets. Theoretically the difficulty can be solved by transferring the foodgrains that these migrants would have consumed in the villages to urban centres. But the release of pressure from dependents who now earn more money in towns and send remittances to relations staying at home enable the latter to consume more food. So no or very little food is available for export from the villages to the towns. If, at the same time, the level of money incomes also rises in the villages, the rural people will tend to consume larger foodgrains, leaving a comparatively smaller proportion of the total crops for sale outside the villages. In other words the marketable surplus, *i.e.*, the quantity of foodgrains sent to the markets for sale may not rise in proportion to the increase in the demand for foodgrains in the urban centres.

Thus the process of economic development generally leads to a large increase in the demand for foodgrains. If the supply or production of foodgrains is not so elastic and cannot be made to increase in proportion to the rise in demand, food prices will tend to rise, increasing the dangers of inflation. This has actually happened in India. In addition to the problem created by the increasing population (which is assumed to be growing at present at the rate of 2·15 p.c. per year),

the rise in the level of money incomes and the faster rate of urbanisation have all combined to drive up food prices. And this also provides an explanation for the fact that in recent times food prices have been rising in spite of the fact that the output of foodgrains has also been rising. The growth in demand has served to outstrip the rise in the production of food crops.

A food plan : A satisfactory food plan depends primarily on measures for increasing the output of crops in proportion to the rise in the demand for foodgrains. The Asoke Mehta Committee (The Foodgrains Enquiry Committee of 1957) have recommended a number of measures for stepping up food production, such as the construction of more major and minor irrigation works, distribution of improved seeds and fertilisers, land reclamation etc. These are well-known measures, and have been recommended by a large number of writers on previous occasions. Increasing the average annual rate of production from 3·2 p.c. to 8·2 p.c. is no doubt an extremely difficult task. But as the Ford Foundation Team observed, this is well within the country's capacity if "an all-out emergency" programme is undertaken. The Third Plan remedied the mistake committed in the drawing up of the Second Plan and the National Development Council had already approved of a total expenditure of about Rs. 1800 crores on items that would go to raise agricultural production ;—an increase of about 80 p.c. over the anticipated expenditure in the Second Plan. The success of this plan would depend to a large extent on the effective management of the different schemes of development and on the proper co-ordination of the work of the various agencies. The problem is really one of improving the organisation of agricultural administration, and of co-ordinating the work of the different departments of the government such as those of agriculture, irrigation etc. Even an efficient use of the existing resources, however inadequate they are, would bring about a considerable increase in food production. A proper food policy should embrace measures for land reform, of improved marketing and credit arrangements, multiplication and distribution of improved varities of seeds, better use of existing water resources and construction of irrigation works, a more extensive use of fertilisers etc. A more forceful programme of agricultural extension education must be effectively carried out in the community development blocks and also in areas not yet covered by such blocks.

A long-term solution must embrace proposals for limiting the growth of population. Through education and propaganda, people should be made conscious of the essential fact that the size of the family has to be regulated in harmony with rationalised individual desires and social needs of the time.

The ultimate solution of the food problem depends essentially on the general economic improvement of the country. An increase in food production depends immediately on the adoption of agricultural improvements ; and the latter, in their turn, must be conceived as an integral part of the much wider problem of raising the level of rural life. Agricultural improvement is inextricably linked up with a whole set of economic and social problems. A solution has to be found in the simultaneous adoption of a two-fold programme,—firstly, increasing the yield per acre by steadily improving agricultural methods and promoting an intensive system of mixed farming ; and secondly, drawing away the surplus population from land into industries through the development of cottage and small-scale industries. large industries and tertiary occupations.

Stabilisation of foodgrains prices : Prices of foodgrains have usually undergone very wide fluctuations. For example, in recent years, the index number of cereals declined from 108 in July 1953 to as low as 67 in May 1955. From that month it has started to rise almost continuously. Such wide fluctuations in foodgrains prices create great difficulties for the cultivators and militate against a programme of increased food production. For this reason the Foodgrains Enquiry Committee have recommended the adoption of a policy of stabilising the prices of foodgrains in this country. Such stability would, in the first place, ensure more or less stable money incomes for the farmers. The principal problem before the cultivators is that if they make strenuous efforts and succeed in increasing the yield of crops, prices may decline to very low levels, and in spite of larger production, their total money incomes may actually decline. Large crops have usually been followed by big drops in prices. Hence farmers may not have much incentive to increase the production of crops. If the government stabilises foodgrains prices and prevents them from falling below particular levels, the farmers need not fear a decline in their money incomes when they try to raise their output. Secondly, when food prices are driven very high, due to, (say), a failure of the monsoons, this proves to be an

important source of inflation in the economy. High food prices raise cost of living and so lead to the demand for higher money wages, and in this way may upset all calculations for planned investment. For these reasons there is a good deal of necessity for adopting a programme for stabilisation of foodgrains prices.

The Asoke Mehta Committee have advocated the establishment of a number of organisations for this purpose,—Price Stabilisation Board, a Foodgrains Stabilisation Organisation, a Central Food Advisory Council and a Price Intelligence Division. The Price Stabilisation Board was to formulate the price policy to be pursued from time to time, and to determine the programme for enforcing it. The Price Intelligence Division would be charged with the duty of collecting all the relevant data and preparing regional price indices for foodgrains. The Central Food Advisory Council was to assist the Price Stabilisation Board on various aspects of the food situation, long-term as well as the short-term. The task of executing the price policy thus decided would devolve upon the Foodgrains Stabilisation Organisation which would be started initially with a capital of Rs. 100 crores, to be increased as and when necessary. This organisation was to undertake purchase and sale operations in the market for the purpose of keeping foodgrains prices within the prescribed limits. It would have a string of warehouses in all important producing and consuming centres.

This was the organisation envisaged by the Foodgrains Enquiry Committee. In addition to the open market sale and purchase of foodgrains by this organisation, a number of other measures have also been recommended by that Committee,—socialisation of a part of the wholesale trade in foodgrains, control over traders operating in the rest of the market through a system of licensing, direct sales of cereals by the government through fair price shops when prices threatened to rise above the permitted levels, formation of zones with a view to prevent cross-movements and undue pressure on local supplies and limited compulsory procurement by the government in surplus areas for replenishing reserve stocks. In addition, the government should make arrangements for the regular import of a certain quantity of foodgrains and organise propaganda for consumption and production of subsidiary food.

These proposals have not been fully implemented by the government, especially with regard to the measures for setting up the various

organisations. There are certain well-known difficulties. A policy of stabilisation of foodgrains prices, however desirable from certain points of view, cannot be enforced during a period of rising foodprices and scarce supplies of foodgrains. Such a situation does not provide much scope for the government purchase of stocks of foodgrains. The latter may be imported ; but that means the using up of another scarce resource, foreign exchange. Moreover, if the prices of only food crops are stabilised, while those of non-food crops are allowed to fluctuate, there may be a tendency on the part of the former to shift from the cultivation of the latter to that of food crops. As a result, the output of important commercial crops may be seriously affected. Lastly, the buffer stocks policy which is the keystone of the scheme of price stabilisation is extremely difficult to operate.

Buffer stocks : The policy of keeping buffer stocks of foodgrains is a very old one. The idea is that when the harvest is ample and prices of foodgrains are declining to very low lefels, the government should buy all surplus foodgrains from the market and thereby prevent prices from falling below particular levels. These crops are to be stored in godowns. When crops fail due to natural calamities and food prices threaten to rise above a certain level, the government is to sell the crops stored in the godowns and so prevent prices from rising. There is no reason why this policy cannot be operated successfully if ample stocks are accumulated during good years and these are sold energetically in the market as prices threaten to rise.

Though the policy has been advocated by the Foodgrains Enquiry Committee, Mr. S. K. Patil, the former Central Minister for Food was an active advocate of the policy of buffer stocks. He succeeded in negotiating with the American government for securing their surplus foodgrains under P. L. 480. These were to form initial stocks for the scheme, supplemented where possible by internal procurement in the surplus areas. The government is already committed to the policy of building large numbers of ware-houses throughout the country and a central warehousing organisation has already been set up for this purpose.

The policy of buffer stocks has an engaging simplicity. The first difficulty is of course with regard to the building up of adequate stocks. If the stocks are to be procured from internal sources, it would need the expenditure of large sums of money to buy all the crops that

would be offered for sale at fixed prices. Is the government in a position to secure enough financial resources for this purpose, in addition to the already very large demands upon its purse for meeting the plan expenditure ? If surplus stocks are not available within the country, as is the situation in 1960-61, these have to be imported from other countries, if the latter possess enough surplus to export. But it would mean a large amount of foreign exchange, which was also very scarce now-a-days. The difficulty can, of course, be solved if one can get hold of a generous foreign government like the U.S.A. which has agreed to supply the foodgrains under P.L. 480 and this does not involve an immediate payment of foreign currency.

Secondly, adequacy of stocks is related to the likely gaps in food supply that may develop in any season. If the gap is due to the operation of ordinary events such as the growth of population and the imbalance between it and the rise in food production, the proper remedy is not buffer stocks, but a deliberate and sustained attempt to raise food production to the required levels. Only when the food gap has been widened temporarily through natural calamities, the buffer stock policy may be of some avail. But in that case the success or failure of the scheme would depend on how large the gap was, and this again would depend on the havoc caused by the natural calamities.

There would be very great administrative difficulties. The success of the scheme would depend considerably on the efficiency and flexibility of the controlling body. And a body consisting of government servants or under the control of the government is not in general in a position to operate in a flexible manner.

There are also other grave defects of this scheme. Under ordinary conditions, when crops fail prices rise. The farmers get low crops, but this is compensated to some extent on account of the high crop prices. When the buffer stock scheme is operated, prices will not be allowed to rise above stated levels, whatever the extent of crop failure. As a result, a farmer who has grown small crops will be put to very great difficulties as he will have to be content with comparatively low incomes. An example would make the position clear. A farmer nomally raises (say) 10 mds of paddy on a bigha of land and sells it at Rs. 10 a maund. His gross-proceeds amount to Rs. 100. When there is a failure of crops, his output declines to only 6 mds. But the price goes up in the market on account of the crop failure, and rises

to Rs. 15 per md. His sale-proceeds are Rs. 90—slightly lower than that under ordinary situations. But if the price is kept within, (say), Rs. 12 through the operation of the buffer stocks scheme, the farmer will receive only Rs. 72. He may of course get more when there are bumper crops and the price is prevented from falling to low levels. But then his average economic condition would depend on the relative numbers of good and bad seasons. If bad seasons outnumber good ones, the farmers would actually fare worse under this scheme.

The present stagnation in agriculture :—The facts about the present stagnation in agricultural production, especially food production, are well-known. In 1960-61, the last year of the Second Plan, total foodgrains production amounted to 82 million tons. In 1965-66, the last year of the 3rd Plan, it amounted to only 72·3 million tons. The maximum output in the 5 years since 1960-61 was only 89·0 million tons in 1964-65. The average output per hectare in 1960-61 of all kinds of foodgrains was 0·71 tons, and it rose to only 0·75 tons in 1964-65, the best year of the 3rd Plan period. In other words, in course of the 4 years of the 3rd Plan, average productivity has risen by about 1·4 p.c. per year, and part of this rise to productivity was due to the increase in the acreage under cultivation. This growth rate in food production is to be studied against the growth rate in population, which is about 2·2 p.c. per year, and a rise in the per capita incomes by about 3 p.c. in these years.

Why is it that, in spite of so much investment in agriculture including irrigation, there has been so little advance in agricultural productivity and so small a rate of return on such investment ? One may admit that the data on average productivity do not provide a correct picture of the rise in productivity that has already been achieved. The attempt to extend the acreage under cultivation has brought large areas of sub-standard soil under the plough, and naturally the yield on these plots will be comparatively low, and the inclusion of such land in the total will bring down the overall average rate of productivity. Even if some allowance is made for this factor, there is no doubt about the extremely low rate of increase in agricultural productivity, especially during the 3rd Plan period.

One favourite explanation for this is the bad monsoons that have characterised the 1965-66 season. Monsoons have no doubt been bad during that season. But what has happened to the large irrigation

projects on which so much investment has been made? These projects were meant to provide some insurance against the vagaries of monsoons, and it seems that they have failed us at the first test. It appears that when the monsoons are unfavourable, these large irrigation projects may not provide us with adequate supplies of water. For, the water supply in the storage dams becomes low and cannot be spared for irrigation purposes if the generation of hydro-electricity is to proceed undisturbed. There have also been many lapses in the administration of these projects so that water was not always available at the right time, in right quantities and to the right plots of land. There have also been failures in the administrative machineries with respect to the distribution of manures and fertilisers among the cultivators. The supply of these fertilisers is no doubt inadequate. But even this inadequate supply has not been properly distributed among the cultivators along with the spread of knowledge relating to their use. The right kind of research—research oriented towards the Indian problems—has not always been carried on in the agricultural research stations, and the organisation to bring the fruits of the research to the doors of the humbler cultivators is yet to be made effective. There has also been a conspicuous failure to bring about appropriate land reforms so that the actual tillers of the soil may have the proper incentive to raise productivity. There are thus a variety of reasons for the failure to bring about the required rate of increase in agricultural productivity.

Questions

1. Discuss the nature of the food problem in India. What measures would you advocate for the solution of this problem?

2. In what respects is the economic development of the country dependent on food production?

3. How do you explain rising food prices in India in recent times? What measures would you recommend to stabilise food prices? (C. U. B. Com. 1960.)

4. Argue the case for and against the following schemes :—
   (1) Stabilisation of foodgrains prices
   (2) Buffer stocks of foodgrains.

CHAPTER 20 COTTAGE AND SMALL-SCALE INDUSTRIES

India was once very famous for her cottage industries. From very early time the skill of the Indians in the production of delicate woven fabrics, in the mixing of colours, the working of metals and precious stones and in all matters of technical arts enjoyed a world-wide celebrity. Even under the rule of the East India Company, there is ample proof to show the excellence of the products of her cottage industries. In 1787 exports of Dacca Muslins to England amounted to Rs. 30 lakhs.

But owing to a combination of circumstances, most of these cottage industries began to decline from the early 19th century. The main factor leading to this decline was the rise of the factory industry in England and later in India. The invention of the powerloom in England completed the decline of Indian industries. A second most important reason was the establishment of an alien rule in India after the battle of Plassey. The English education and the influence of foreign rulers led to a change in the tastes and fashion among Indians. As a result, the new aristocracy ceased to patronise Indian goods and switched over to foreign goods. The nawabs and courtiers of early days used formerly to patronise and support the artisans. They began, however, to imitate the British rulers, and this had an adverse effect on the fortune of the cottage industries. The policy pursued by the East India Company was also an important factor. Under the pressure of the British Government the company began to discourage the export of Indian manufactured goods to Europe, and they refused to adopt the policy of protection for the Indian industries when machine-made goods from Great Britain flooded the Indian market. The result of the operation of these factors was the decline of a large number of cottage industries.

Definition of cottage industies : Before one proceeds further to examine the economic position of cottage and small-scale industries, it is necessary to define these two terms clearly. Without entering into lengthy discussions on this point it is best to follow the definitions given in the Report of the Fiscal Commission of 1949-50. The Commission defined a cottage industry as one which is carried on generally in the home of artisan himself or in small karkhans wholly or primarily with

the help of the members of the family, either as a whole-time or part-time occupation. A small-scale industry, on the other hand, is one which is operated mainly with hired labour, though the number of such workers is small. From a technical point of view, small-scale industries belong to the same genus as large-scale ones. They differ from the latter mainly in regard to the number of workers employed. The distinction between a cottage industry and a small-scale industry lies in several factors. The most important is the fact that in a cottage industry, work is done mainly by the members of the family of the artisan with probably a few hired workmen. In a small-scale industry, the workers are mainly hired. Secondly, "cottage industries are generally associated with agriculture in rural areas and provide whole-time occupation only in urban areas ; small-scale industries generally provide whole-time occupation to their workers and are located in urban or suburban areas." This definition is of course not entirely satisfactory. But it will do for our purpose.

Classification : The industries have been variously classified. The most usual classification is between rural and urban industries. Both these groups of industries may further be sub-divided into those providing part-time and whole-time occupations. Part-time rural cottage industries provide supplementary occupation to agriculturists, *e.g.* basket-making, bidi-making, handloom weaving etc. Wholetime rural cottage industries consist of the well-known village crafts such as pottery, blacksmithy, carpentary, oil-pressing by ghanis, tannery, cart-making, hand-loom weaving etc.

In urban areas, cottage industries consist of handloom weaving industry, brass and bell metal industry, toy-making, wood and ivory carving industry, gold and silver thread industry etc.

There are also rural and urban small-scale industries. There are a small number of small-scale industries like rice and flour mills, khandsari factories, gur-making etc., which provide part-time occupation to agriculturists. Small-scale industries which provide whole-time occupation in rural areas are extremely few in number.

In urban areas, there are small-scale industries of a seasonal nature like brick-making, which engage part-time labour ; and others like small hosiery plants, engineering factories etc., which provide wholetime occupation to a large number of people.

The Report of the International Planning Team sponsored by the Ford Foundation has classified these industries into two broad groups, *viz.*, (a) traditional cottage industries in the rural areas working primarily to meet the needs of the village itself and only occasionally for the nearby village or small town markets, and (b) small industries including traditional artistic crafts aiming at selling in larger markets, both at home and abroad.

Some important cottage industries : Among important cottage industries mention should be made of the handloom industry, the silk industry, the woollen industry, pottery, glass bangles industry, brass and bell metal industry etc.

Handloom industry : Next to agriculture, the handloom industry provides employment to the largest number of people. According to the Factfinding Enquiry Committee of 1941, there were about 20 lakh handlooms in India. About fourth-fifth of India's textile industry's labour are employed in this industry. The total production of handlooms (including power looms) has been estimated to amount to 2112 million yards in 1960, *i.e.*, about one-sixth of the total mill production.

Organisation : There are many peculiarities in the structure of this industry. At one end there are independent weavers operating one or a few looms and at the other end there are small *karkhanas* operated by financiers and employing wage workers. "In fact, the handloom industry to-day presents a pageant of all the known stages in industrial evolution." The number of independent weavers is, however, declining, and it is only in Assam, Bihar and to some extent in Madras that a great majority are still independent weavers. In Assam most of the weavers are women and they carry on weaving chiefly for home use. In a large majority of cases, these weavers obtain their raw materials from dealers on credit, and sell their cloth either to the mahajans or at the local *hats*. In areas where production is largely for distant markets and the weavers are financially weak, they have become employees of merchants or *sowcar*-weavers, although working in their homes ; in other places they have been congregated in small workshops called karkhanas. The latter change has happened more in Maharashtra and Madras than in Northern India. Some of these *sowcar*-weavers and karkhanas have built up very large organisations in centres which cater for export markets. Thus in many areas a class of small entrepreneurs, working either as mahajans in small factories or as karkhanadars with

labour engaged in small factories is playing a large part in the production and marketing of handloom cloth.

There are two other peculiarities of this industry to which the Factfinding Committee has drawn attention. In the first place, contrary to popular expectations, the industry does not provide subsidiary occupation to agriculturists. On the other hand, the great majority of weavers, with the exception of Assam, are full-time workers. What is subsidiary in their case is not weaving but agriculture. Secondly, the industry is essentially an urban industry except in backward tracts of the country. In Bombay 45 p.c. of the total looms are found in 26 urban centres ; in Madras 39 p.c. of the looms are found in 49 urban areas. Moreover, though a large number of weavers are still residing in villages, they usually have little connection with agriculture.

With a large number of weavers working in urban areas, a good many subsidiary industries like dyeing, bleaching and finishing, gold and silver thread making and embroidery etc., have also sprung up in the vicinity. In this manner a certain degree of localisation of industry had taken place. Side by side with such localisation some amount of geographical specialisation has also taken place. For example, Dacca had always specialised in artistic cotton saris like jamdanis. Santipur and other centres have also been noted for special types of fabrics. Many centres in Western India such as Ahmedabad, Surat and Yeola specialised in the making of gorgeous fabrics. While the above centres specialised in cotton fabrics, others like Murshidabad and Vishnupur in Bengal, Banaras and Man in U.P., Conjeevaram and Madura in Madras concentrated on silk.

Among the States, Madras produces the largest quantity of handloom cloth. Four districts in that State contain more than 5,000 looms per 1,000 sq. miles. Four districts in Maharashtra—Surat, Sholapur, Bijapur and Dholka—contain between 2,000 and 4,000 looms per 1,000 sq. miles. In West Bengal, two districts (Hooghly and Howrah) containing more than 4,000 looms per 1,000 sq. miles. In U.P., five districts (Bijnoor, Moradabad, Jalaun, Banaras and Azamgarh) have more than 4,000 looms per 1,000 sq. miles.

Present position and defects : Though after more than hundred years of mill competition the handloom industry still employs a large number of men, the economic condition of weavers is far from

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satisfactory. The present earnings of weavers are extremely low, and a large number of them are facing the threat of unemployment. Moreover, they are heavily indebted. The weaver has only a limited market and he has often to sell his cloth in the bazar at whatever price he can get because he cannot wait. There is no marketing organisation to sell the products of this industry at reasonable prices. In the case of independent weavers credit has to be obtained at a high charge. Under the stress of competition the quality of handloom cloth has deteriorated in certain places and consequently there have been complaints from consumers regarding dimensions, weight, ends and picks per inch etc., injuring the reputation of handloom products. Lastly, in a large number of cases the ignorance and conservatism of the weavers make them disinclined to adjust their lines of production and types of designs to suit modern tastes. Hence the handweaver's production cost is bound to be higher, and he is facing a declining market.

Prospects and advantages: As against these unfavourable factors, one must take account of the fact that though this industry has almost disappeared in a large number of countries during the last 100 years, it has not done so in India. This shows that this industry has a unique capacity for survival. There are several reasons for this. In the first place, the industry possesses commendable capacity to adjust itself to changing conditions. The weavers have adopted modern implements like fly-shuttle sleys, dobbies and jacquards etc. They have tried to follow changes in popular tastes and have adjusted their workmanship to modern requirements. Secondly, the capital cost and the running expenses of the handloom weaver are small, and he has not to worry about depreciation, insurance, income tax, strikes and lock-outs which weigh heavily on mills. Thirdly, the help of family members economises expenses. The weaver, wife and children have each their parts to perform without any great burden on any of them. Fourth, the weaver has another advantage as he can weave delicate fabric using high count yarn with complicated designs and cloth of striped and checked patterns. The great merit of high-class handloom products is their distinctiveness and delicacy of workmanship. Lastly, another favourable factor is the general belief that hand-woven cloth is more durable, and therefore, cheaper in the long run than mill-made cloth. It is quite clear that the handloom industry can still hold its own and prosper if only a little aid is extended to it. In the words of the Fact-finding Committee, the

position of the industry is such that it needs only a little help and not a bolstering up.

Suggestions for helping the industry. In view of the great importance of this industry, there is no doubt that its claim to state aid is not less supportable than that of any other industry. The chief problems facing the weavers are the high cost of raw materials, difficulties and the cost of getting credit, and the absence of good marketing organisation. What they require most is an organisation for the supply of yarn and dyes at reasonable prices, for finding new designs more in accord with modern tastes, and for facilitating the flow of credit at reasonable rates, and for selling the product at home and abroad. That organisation should try to popularise the handloom products in different markets, internal and foreign, and arrange for research on various aspects of the industry. The government has already set up an All-India Handloom Board to which financial assistance is being given. The Board has framed ambitious schemes for the marketing of handloom cloth abroad with the help of marketing officers and opening up emporia in foreign countries. It has also framed plans for stepping up the internal market for cloth. The need for introducing quality standards for handloom cloth is also being increasingly recognised.

Much can be done by the co-operative method. Co-operative societies may help in the procurement of raw materials and marketing of cloth. These may also be organised for the supply of credit and mobile co-operative banking units may help the weavers in getting finance at reasonable rates. It is only co-operative organisations that can finance and establish common plants for certain processes like dyeing, calendaring and bleaching.

It is also very necessary for the weaver to take full advantages of the latest improvements in the technique of production. Throw-shuttle looms should be replaced by fly-shuttle looms and pedal looms. There is also an equal need for adopting new and changing designs to suit the tastes of the modern customers. Good design and technical quality are two most urgent needs for the revival of the handloom industry.

State aid to the handloom industry. Recognising the importance of the handloom industry, the government has recently adopted certain proposals to help the development of this industry. The first step in

this direction was the establishment of the All-India Handloom Board in October, 1952 to stimulate the development of the industry on sound lines. The Central Government has also imposed an excise duty of three paise per yard on mill cloth, and this was expected to yield an annual revenue of about Rs. 6 crores. This money is being utilised for assisting the handloom and khadi industries. Thirdly, an internal marketing organisation with a central marketing body and a number of branches in important cities in India has also been set up. An External Marketing Organisation with a net-work of Marketing Officers and Sales Emporia covering the Middle-East and South-East Asian markets has also been established. Fourthly, the Handloom Board are making experiments with new types of looms and equipment intended to augment the output of handloom cloth.

The States have also adopted a number of measures to this effect, and these schemes are being financed by grants sanctioned by the central government. West Bengal, for example, has received an interest-free loan of Rs. 54,000 to be utilised for the establishment of 12 regional dye-houses in the State. Bihar has also received some grant for setting up a Handlooms Research and Design Centre. Other States have received grants for opening sales depots etc.

Other cottage industries : In addition to the handloom industry, there are the silk industry, the woollen industry, pottery, oil industry, rope-making industry, embroidery and lace-making industry, glass industry, paper industry etc. We shall give brief descriptions of some of the more important industries.

Silk industry : Like the handlooms, the silk industry was once in a very flourishing state. But the competition of mill-made products, the change in popular taste and the withdrawal of the patronage of the rulers and noblemen led to the decline of this industry. In recent times the competition of artificial silk is proving to be a serious factor. Important centres of silk-weaving are to be found in Assam, Bihar, Madras, Punjab, U.P., West Bengal, Mysore and Kashmir. Banaras in U.P. is famous for its silk saries and has a large and highly skilled weaving population plying about 25,000 looms. Bhagalpur in Bihar is noted for tassar silk. Murshidabad and Bishnupur in West Bengal, Berhampur in Orissa, Sualkuchi in Assam, Bangalore in Mysore, etc. are also noted centres of silk-weaving.

This industry has also received the attention of the government which has set up a Central Silk Board to promote the development of this industry. A change in popular taste in favour of Indian silk goods, and high import duty on foreign products have given some stimulus to this industry.

Woollen industry : This is also an old industry. Its main products are shawl, carpets, blankets etc. Shawls of Kashmir are very famous throughout the country. Though the prosperity of this industry has declined in recent years, it still holds an important place. The Kashmir government is spending considerable sums of money for its improvement.

The carpet-weaving industry made large advances during pre-British days. But it has declined materialy owing to the popularisation of artificial dyes, and introduction of cheap designs under the influence of foreign markets. At present the main centres of production are Kashmir, Amritsar, Mirzapur and Gwalior. Srinagar and Amritsar have specialised in the production of costlier products, while Mirzapur and Gwalior turn out cheaper and rough products. The manufacture of rough blankets, known as *Kambalis,* is also carried on in U.P. and other states.

Pottery : This cotage industry is carried on in almost every village in India to meet the demand of the people for earthern wares like surahis, handis gharas etc. Clay dolls are also manufactured in many places, the most important centre in West Bengal being Krishnagar.

Embroidery and lace-making : Important centres of this industry are Lucknow in U.P., West Godavari in Madras, Darjeeling in West Bengal etc. Now-a-days this industry is in difficulties though efforts are being made to revive it.

Glass industry : This is also one of the most ancient industries of India. The most famous centre is Ferozabad in U.P., where "shisagars" are justly noted for their bangles and other glasswares. Besides Ferozabad, glasswares are also manufactured in West Bengal, Bombay, M.P., Punjab and in Madras. Hathras in U.P. is also noted for producing glass battons, animal figures etc.

Paper industry : Manufacture of paper by hand existed in India from very early times. But it has almost disappeared owing to the

competition of machine-made products. Of late attempts are being made to revive it. Chief centres of production are Madras, Andhra, U.P., Manipur, Bombay and Kashmir. The All-India Village Industries Association is trying to revive this industry.

In addition, there are brass and bell metal industry, manufacturing kitchen utensils and other wares, oil industry manufacturing vegetable oil in *ghanis,* mat-making industry manufacturing mats from Korai reeds, palmyra and date leaves etc.

Problems of cottage and small-scale industry : The problems and difficulties faced by those industries can be classified into four groups. First, the antiquated technique of production followed in many of these industries and the old implements are a major stumbling block in the way of their revival. Secondly, lack of adequate financial facilities at reasonable cost is also a great impediment. The artisans are usually very poor and do not possess the resources to buy good raw materials and to hold out for better prices. They are heavily indebted to the *sowcars* and have to pay high interest charges and in many cases to sell the finished products to the mahajan dealers where they cannot always be sure of getting proper prices. Thirdly, another serious defect is the absence of any marketing organisation to sell the products of these industries both at home and abroad. Lastly, due to their illiteracy and conservatism, the artisans have not moved with the times, nor do they always appreciate the need of introducing better designs and finish more in accord with modern tastes. There is no doubt that on account of a combination of factors, these industries are to-day facing a crisis, their number of employed workers and their output of production gradually declining and in some cases slowly grinding to a halt.

In order to infuse new life into these industries it is essential that these problems should be attacked on a systematic basis. A proper policy for reviving these industries should start from the market end. We must first find out what articles will sell and at what prices. Then comes designing. How should the products of these industries be designed, made and finished so as to attract a large market ? The next task should be to provide for the supply of better raw materials, better equipment, better power facilities. These questions have to deal with the organisation of production, research and technical aid. Lastly,

one must attack the problem of providing for adequate financial facilities. All this should be conceived as an integrated plan, to be carried out simultaneously on all fronts.

That something has already been done has been noted in the section on the state aid to the handloom industry. In addition to the All-India Handloom Board, the government has also set up the All-India Khadi and Village Industries Board and the All-India Handicrafts Board for the purpose of stimulating the development of cottage and small-scale industries. In addition, there are two other Boards, the Central Silk Board and the Coir Board, dealing with these two industries. Grants totalling about Rs. 6 crores have been given to these institutions during the 5 years ending 1953-54 to enable them to finance various schemes. The Five Year Plan includes provisions for spending Rs. 27 crores (Rs. 15 crores by the centre and the rest by the states) for the development of these industries. The All-India Khadi and Village Industries Board has chalked out a detailed programme for the development of such industries as soap-making with neem oil, leather industry, hand-made paper, hand-pounding of rice and bee-keeping. Some marketing organisations are also being set up to encourage the sale of the products of these industries.

Recommendations of the International Team : It will be helpful if we review at this stage some of the important recommendations of the Ford Foundation International Planning Team on small industries. The Report of this team has recommended the establishment of at least four Institutes of Technology, at different regions in India to initiate and carry on investigation as to the existing methods of production, to conduct applied research for providing the development of these industries and to disseminate the methods and results thus obtained among the artisans and industrialists through mobile demonstration units and travelling industrial extension workers. Secondly, to improve the design and technical quality of the products, a National School of Design should be set up to serve as a centre for creative studies in design and fashion. The basic functions of this school would be to prepare improved designs suitable for commercial production. In addition, a Customers' Service Corporation is also to be organised to conduct continual survey of current production, to gather samples and information from Indian and foreign buyers. This organisation should thus serve as a liaision between producers and consumers. To improve

the marketing organisation, Export Development offices should be set up in different parts of the world to promote and stimulate foreign trade in handicrafts and to serve as contacts with foreign buyers and their demands. To improve production and to maintain standards, it would be best to promote the organisation of trade associations, *i.e.*, voluntary associations of members of a given industry or trade. The Central and State Governments should take the initiative in promoting the formation of such associations which would help members with new methods and techniques and also serve as information centres to their members.

To solve the problem of finance, the team has made a number of recommendations. First, the commercial banks should delegate more authority to branches to make loans to small business, and generally try to decentralise their loan business. Secondly, a system of loans against the security of real-estate mortgages should be considered and developed. Thirdly, all States should set up State Finance Corporations with a portion of their funds set apart exclusively for small industries. Fourthly, co-operative banks should expand into the industrial field. The Central Government should also organise a Small Industries Corporation. The primary purpose of the Corporation would be to provide the necessary incentive and help small industry to improve its technique of production and management by working on assured orders for the government. Its basic function would be procurement with power to pre-empt at least 25 p.c. of government indents at prices substantially equal to those offered by the general business community.

Lastly, marketing developments should proceed along these lines. First, products of these industry must be made good and of uniform quality. Secondly, they must be so made as to meet the customers' felt needs. Thirdly, aggressive efforts are to be made to reach and stimulate the huge potential markets of the villages and urban areas. With these ends in view, the government should set up a Marketing Service Corporation, to find out the nature and extent of consumer demands through surveys, encourage producers to meet these demands and secure and process orders from wholesalers and retailers. This Corporation should set up a marketing news service, establishing contacts and reporting liaision with all principal foreign and domestic markets.

The Team also recognised that the co-operative movement may help the development of these industries in many ways. Co-operative

societies may help in procuring raw materials and the marketing of finished products. They could also help in the provision of credit. Mobile co-operative banking units may provide a partial answer to helping small village industries obtain credit for modernisation.

These recommendations are highly valuable and will, if carried out, solve many of the problems of the small-scale industries.

Choice of techniques of production : Small and large industries : There is no doubt that small-scale and cottage industries occupy an important place in the Indian economy. Those who argue that it is useless to spend money on the development of these industries as they are bound to collapse in the face of the competition of large-scale industries fail to take account of all the relevant factors. As the Fiscal Commission pointed out in its report, it is not always true to say that the costs of production are usually higher in these industries than those in the large-scale industries. In the first place, while manufacturing costs may be higher in the small-scale industries, this handicap may be partially offset by the relatively low cost of distribution. A cottage or small-scale industry is better able to adjust the nature and quality of its output to local demand in view of its small size and its close touch with the local market. Secondly, modern trends of technological progress are tending to redress the balance in favour of certain types of cottage and small-scale industries. The use of electric motors and internal combustion engines has reduced the economic scale of production units in certain lines of production. Thirdly, the scale might turn in favour of cottage and small-scale industries when we take account of the "social costs" of large industries. The costs of large investments in projects like housing, public utilities etc. which are essential in the case of large industries may be avoided in the case of these industries as these will be located mostly in rural areas or near the homes of the workers.

That these industries are not handicapped from the point of view of cost of production is borne out by their vitality even in the industrially advanced countries. For example, in the U. K., business units employing between 5 and 30 persons produced 19 p.c. of the total output and employed 29 p.c. of the total working population in that country. In pre-war Germany, small establishments employing 5 persons formed 22·3 p.c. of the total number of establishments. In

Japan, small plants employing less than 5 workers employed 53 p.c. of the total number of workers in the country. In the U.S.A., traditionally a country of large business, "small business makes up 92·5 p.c. of U.S. business establishment, employs 45 p.c. of the country's workers and handles 34 p.c. of its volume of business." Thus these industries occupy a significant place in the economy of these countries, and there is no reason to expect that the case need be otherwise in India.

There are also additional considerations in favour of these industries. As is well-known, labour is cheap and abundant in India, while capital is dear and is inadequate in supply. In such a country, labour-using and capital-saving occupations have a special function to discharge. These industries exactly fit in with such requirements. One of our principal economic problems is the large-scale unemployment existing in the country. The development of large industries over the last century has not proved much effective in solving this problem. Even if large industries are developed at a faster rate, it is doubtful whether they could provide occupation for more than a million or two of the workers. This would still leave a large number of unemployed. Thus from the point of view of securing maximum employment in a capital-scarce country, small-scale and cottage industries have an important part to play in our economic life.

Moreover, small-scale industries mean decentralised production, and the latter has certain advantages. In the first place, such decentralised production has important military and tactical advantages. The enemy can destroy centres of large-scale industries but cannot harm small-industries scattered all over country. Secondly, decentralised production will result in a wider diffusion of purchasing power among the people. The growth of large-scale industries has everywhere resulted in an extremely unequal distribution of income.

Lastly, there is another special reason for the preservation of small-scale industries. This is of course mainly social and only partly economic. If large-scale industrialisation involves the decay of village crafts and the concentration of workers in cities, the inherited skill of our artisans will be lost and the lives of the people will become mechanical and monotonous. One should not under-estimate the importance of such social factors because they exercise a great and abiding influence on the economic life of the country.

Financing of Cottage and small-scale industries : The importance of these groups of industries will be obvious from the fact that according to the estimates of the National Income Committee, the value of the net output of small industrial units was Rs. 910 crores in 1950-51 as against Rs. 550 crores in the case of factory establishments. They employed 11·5 million workers against 3 million employed in the large industries.

There is hardly any effective organisation to supply their credit needs. They are generally too small to be in a position to tap the money market for funds through the sale of shares or debentures. They have, therefore, to rely mostly on their own resources, which are undoubtedly small and inadequate, and on borrowed capital. (*a*) The artisans, for example, have to borrow heavily from the *sowcar-mahajans* or dealers. (*b*) The small units also borrow from the indigenous bankers. These are expensive sources as the loans carry high rates of interest or other onerous conditions. (*c*) In some cases co-operative banks granted loans to small concerns. But the co-operative movement has not so far paid much attention to the organisation of industrial societies. In West Bengal, for example, out of 7 lakh workers engaged in cottage and small-scale units, the total membership of industrial co-operative amounted to hardly 65,000 in 1950. Moreover, co-operative finance is available only on a short-term basis. (*d*) Commercial banks do not generally lend to these concerns. Banks possess limited resources and the demand in the organised markets is more than sufficient to absorb their funds. Moreover, in view of the comparatively weak structure of these units, they are mostly not in a position to offer satisfactory securities as collateral for bank loans.

In view of the inadequacy of these resources. the State had to come to the aid of the small units. (*e*) Almost every State has passed a State Aid to Industries Act under which State governments offered long and medium-term credit to small industrial units. But so far the amount of such aid has been insignificant. For example, in 1953-54, West Bengal made provision for only Rs. 3 lakhs in its budget on this account, Madras only Rs. 12 lakhs and Mysore Rs. 7 lakhs. However meagre these amounts are, the actual sums disbursed are even less. There is usually a long delay in sanctioning, and the payment of, a loan, and this often discourages potential borrowers. The provisions of these acts are unduly rigid and the procedure for granting loans is unneces-

sarily lengthy and these facts militate against the grant of adequate and timely financial accommodation.

State Finance Corporations : It has been proposed for some time that while the Industrial Finance Corporation, set up by the Government of India, is designed to provide long-term finance to large units, the States should establish State Finance Corporations for financing small-scale and medium-size units. To facilitate the establishment of such Corporations the Central Government passed a State Finance Corporation Act in 1951. The Act is an enabling Act providing for the establishment of State Financial Corporations in different States. The share capital of each Corporation is to be fixed by the State government, subject to a minimum of Rs. 50 lakhs and a maximum of Rs. 5 crores. The public may be allowed to subscribe to the shares to the extent of a maximum of 25 p.c., the rest to be subscribed by the State government, scheduled banks, co-operative banks, insurance companies and other financial institutions. As is the case of the I.F.C., the Corporation can accept fixed deposits to be kept for a minimum period of 5 years, issue bonds whose aggregate amount is not to exceed 5 times the paid-up capital and reserve funds. These bonds as well as the share capital are to be guaranteed by the State governments as to the repayment of the principal and payment of interest or dividend. The Corporations are (a) to grant loans and advances repayable within 20 years, (*b*) to guarantee the loans floated by industrial concerns and (*c*) to underwrite the issue of shares, bonds or debentures on the same terms as the I.F.C. The maximum amount to be lent to any concern is not to exceed 10 p.c. of the paid-up capital of the Corporation or Rs. 10 lakhs, whichever is less.

Fifteen States including West Bengal, Punjab etc., have established such Corporations. These have started their work, and from the manner of their working it is evident that for sometime to come. the financial assistance they may provide will not be appreciable. As the reports of a number of Financial Corporations show, the scope of their activities is considerably restricted. They can provide financial assistance only to those selected industries which are organised and are able to offer tangible assets as security. Whereas most of the small industrial units are only loosely organised. They are owned by joint families or partnerships or single members. In many cases joint families are broken up without proper partition deeds ; partnerships are made and unmade,

without dissolution deeds or documents showing the settlement of accounts between partners. Many of these concerns are indifferent to the maintenance of accounts and other records according to accepted standards, and where some sort of books are kept, they are in the nature of scrolls from which it is impossible to know the exact position of the concern. In view of these facts, it is difficult to see how far the mere organisation of State Finance Corporations would solve the problem, as they can deal only with concerns which have a well-defined constitution and status.

There is, moreover, the danger that the indiscriminate establishment of too many State Corporations might result in a mere locking up of available funds by them rather than providing these industries with funds. It would be better if two or more adjoining States jointly start a State Finance Corporation. These Corporations should earmark a portion of their funds exclusively for the use of small industries for ordinary loans.

State Industrial Development Corporations : A number of States have recently set up State Industrial Development Corporations (SIDC) under the Indian Companies Act to provide more financial assistance to small industries. So far eleven such institutions have been set up in the States of Andhra Pradesh, Bihar, Guzarat, Kerala, Madras, Madhya Pradesh and U.P. In addition to the usual activities relating to the grant of loans and advances, underwriting of shares and debentures, guaranteeing of loans etc., some of the SID'S have been authorised to develop and manage industrial estates, to undertake the generation, transmission and sale of electricity in specified areas. They can render aid in supplying machinery on hire-purchase, and participate in equity capital in selected small-scale industrial units. They are expected to combine in their operations the functions of financiers as well as those of promoters and welfare bodies.

Other measures : Another measure that has been suggested by this Shroff Committee is to set up a Special Development Corporation to provide long-term finance to small industries. This Corporation should take a lead in organising small industries and rendering assistance to them in the matter of joint or co-operative purchase of raw materials. organised marketing etc. The recommendations of the Ford Foundation Team, already noted, are also worth serious consideration.

The commercial banks should delegate more authority to branch managers to grant loans to small units, and wherever necessary, they should set up Local Advisory Boards to examine applications for loans. The government should also consider the adoption of a sound system of instalment credit for financing the purchase of modernised machinery, tools and other equipments by those who want to set up small industrial units.

Much can also be done by paying more attention to the organisation of industrial co-operatives among the small producers and artisans. It is essential that co-operative banks should expand into the industrial field.

Recently the Central Government has liberalised the rules for the grant of loans to small industries. It has agreed to place larger funds at the disposal of the State governments to enable them to grant loans under the State Aid to Industries Act on liberal terms. According to this Scheme loans up to Rs. 50,000 would be granted both for working capital and fixed capital requirements at the rate of 3 p.c. for a period of 10 years. Such loans can be given up to 75 p.c. of the value of securities offered and such security should include not only land and buildings, plant and machinery, but also stock-in-trade and finished goods. Loans up to Rs. 1,000 can be granted on purely personal bonds. The Central Government has also agreed to share the losses on such transactions.

Following the recommendations of the Hyderabad Seminar on Financing of Small Industries, the Reserve Bank has given effect to the scheme for guaranteeing loans to such industries. The Reserve Bank as the agent of the Central government has undertaken to guarantee the advances granted to small industries by a number of approved credit institutions including the State Bank of India, 49 commercial banks, 22 State Co-operative Banks and the 15 State Financial Corporations. The scheme provides for a sharing of the losses sustained by these institutions on their loans to small industries between the lending institutions and the Government of India.

Apart from such direct financing, the central government has suggested to the State governments that the latter should introduce a system of guarantee of repayment of not more than 75 p.c. of the funds advanced by the commercial and co-operative banks to the small-scale

industries or industrial co-operatives. If the State government suffers any loss, the Central government would meet 50 p.c. of this loss.

The State Bank of India has also introduced schemes under which the branches of the State Bank would act as the agent for co-ordinating the activities of the co-operative banks, commercial banks and the State Financial Corporations with regard to the grant of loans to small-scale industrial units. The latter would be required to submit loan applications to the Agent of the State Bank in all cases where the applicant is not a member of a co-operative bank. If the applicant wants small loans, this will be granted by the State government under the State Aid to Industries Act. Short-term loans against marketable securities are to be granted by the State Bank and the Co-operative banks. Medium-term and long-term loans and other short-term loans are to be granted by the State Financial Corporations. The State Bank also acts as the agent of the latter with regard to the preliminary enquiries. In this way an attempt was being made to co-ordinate the activities of the different institutions working in this field and to ensure a smooth flow of loans to the small industrialists.

Relation between cottage and small-scale industries and large industries : Many of the supporters of cottage industries have argued that these should be granted protection in certain ways against the competition of large-scale factories. They draw attention to the injury caused to cottage and small-scale industries by the competition of large-scale industries. In their opinion some restrictions should be placed on large factories for the protection of the markets of small industries. This raises the question of the proper relationship that should exist between these two types of industries.

At the outset it is necessary to state that not all cottage and small-scale industries are in competition with large factories. In the first place, there are a larger number of small industries whose continued existence depends on the supply of materials or components for large factories, *e.g.*, tape-making, motor cushion making, bobbin making etc. Secondly, there is a considerable field where cottage and small-scale industries can carry out many of the processes incidental to large-scale methods of manufacture. For instance, factory-made splints and venears could, under proper conditions, be economically utilised in cottage industries to manufacture matches. It is well-known that a

good deal of factory production in Japan and Switzerland is carried on by this method. Lastly, in regard to those cottage industries which produce artistic, semi-luxury or luxury goods, competition from large-scale industries is almost non-existent. There are also a number of cottage and small-scale industries which may be established in the rural areas. There are primarily concerned with processing local produce and selling in a predominantly local market. With some modernisation these can stand the competition of large industries.

These are, however, fields in which both large-scale and small industries are in competitive position. Even in a large number of these cases, a modernised cottage industry may safely hold its own against large factories. Emphasis should, first of all, be placed on improving and modernising a cottage or small-scale industry so as to raise its competitive efficiency. In cases where it is felt that a particular cottage or small-scale industry cannot develop without some form of protection against large-scale factories, the government may take such steps as delimitation of the field of production, delimitation of markets, levy of differential excise duties, differential freight rates etc., in order to safeguard the position of small industries until the competitive position of the latter improves as a result of modernisation. When new large-scale factories are planned, and apply for licence, the government should conduct investigation as to what processes in relation to these industries could be manufactured in small-scale establishment and fix the location of factories in such a way as to permit of this type of decentralisation.

What is now wanted for the solution of this problem is a positive and dynamic policy aimed at improving the facilities for production, finance and marketing for the cottage and small-scale industries. Their difficulties can be solved only by efficient organisation, marketing and research.

Improvement of small-scale industries : Following the recommendations of the International Ford Foundation Team, the Government of India has set up the Small Industries Board with the object of promoting small-scale and medium-sized industries, engaged mostly in the manufacture of consumer goods. This Board has taken a number of steps for the improvement of these industries. In the first place. four regional Small Industries Service Institutes (SISI) have

been established at Calcutta, Bombay, Madras and Delhi. These Institutes are carrying out the policy and programmes laid down by this Board. In addition, the National Small Industries Corporation (NSIC) has been established by the Central government with an authorised capital of Rs. 1 crore. The principal object of this Corporation is to secure contracts for government supplies and to sub-contract them to the small-scale industrial units. The Corporation will advance loans and provide the necessary technical assistance to enable these units to execute the orders. Another important measure adopted by the Board is the introduction of hire-purchase schemes for making the necessary machinery available to the small industrialists. Under this scheme, the small industrialist is required to deposit only 20 p.c. of the value of the machinery, while the other 80 p.c. is found by the National Small Industries Corporation.

The Small Industries Board is also trying in other ways to improve the working of small units. It has adopted several measures for ensuring the supply of proper raw materials in sufficient quantities to these units. It has also come forward to grant subsidies to small industrial units to compensate them for the higher cost of electricity in places where the tariff for electricity charged for small industries is much higher than for large industries.

Other steps which are being actively pursued are the provision of common facility centres, quality marking schemes and the establishment of industrial estates. The small industrialist cannot afford to have costly servicing centres such as for wood seasoning, metal testing etc. These involve heavy capital expenditure, such as the installation of precision instruments etc. As such, the small industrialist cannot afford to have such facilities. The Small Industries Board has recommended to the State Governments that they should provide such common facility centres in places where the small industries are concentrated so that the latter may secure such services at the reasonable cost to them without having to invest large sums of money. The State Government have also been requested to introduce a scheme of quality marking in places where small industries are concentrated so that the quality of their production is maintained at the level of standard specifications.

The scheme of setting up industrial estates is also being adopted in a number of centres. Industrial estates are selected areas where

work-sheds are constructed by the Government or by a specially constituted Corporation. These places are generally close to rail heads and facilities like water, light, post office, railway siding, transport etc. are provided by the authorities. The premises are let out to an enterprising industrialist on a monthly rent. Under this scheme, enterprising small industrialist can embark upon his business with a very small capital. Steps have been taken to establish a number of such industrial estates all over the country. By the end of 1962, 92 industrial estates had been set up. and 121 were in different stages of construction.

During the 1st and 2nd plan periods, the various governments have spent Rs. 218 crores for the development of these industries. In the Third Plan, Rs. 264 crores have been provided out of which Rs. 34 crores are to be spent on handlooms and Rs. 30·2 crores on industrial estates.

An important step is the planned development of small industries as ancillary to big industries. The latter should seriously consider the principle of sub-contracting, *i.e.*, handing over the production of certain parts to small industries in their neighbourhood. The main commodity (for example, a cycle) may be manufactured most economically in a large factory. But certain parts of that commodity can be handed to small units for manufacture, as such things are manufactured in small industrial units more economically than in the large businesses. This would provide for the simultaneous development of both large and small industrial units and would also help the dispersal of industries.

Questions

1. Examine the causes of the survival of cottage industries. (C. U. 1936, 1930.)

2. Describe the structure and present position of the handloom cotton industry.

3. What difficulties are being experienced by the handloom industry in India to-day ? What steps have recently been taken by the government to improve this industry ?

4. What means would you suggest to improve the efficiency of the handloom industry ?

What steps would you suggest for improving the competitive capacity of small-scale industries ? (Bom. 1953.)

5. Examine the importance of cottage and small-scale industries in the industrial structure of India. (Bom. 1952, Mad. 1953)

6. Examine the present system of financing for small-scale and cottage industries. What steps would you suggest for improving the present system? (C. U. B. Com. 1960.)

7. Comment on the proposal which heave recently been made to delimit the spheres of production of handloom and mills.

CHAPTER 21

SOME LARGE-SCALE INDUSTRIES

In this chapter we are going to study the course of development of the more important large-scale manufacturing industries in India.

Cotton textile industry : This is probably one of the oldest large-scale manufacturing industries of India. The first cotton mill was started as early as 1818 in Calcutta. But the real development came after 1854, when a cotton mill was set up in Bombay. Since then the development has been continuous, though the pace was not uniform in all decades. This industry is notable on account of the fact that it has been developed to its present stature by Indian capital and management against powerful foreign competition, and in the face of the indifference and sometimes, the hostility of the British Government in India.

The industry occupies a unique position in the industrial organisation. The capital invested in the industry is estimated at Rs. 136 crores and the annual turnover is between Rs. 350 to Rs. 400 crores. It provides employment to more than seven and a half lakh workers. It produces 14 p.c. of the estimated world production of cotton cloth and 13 p.c. of the production of yarn. The industry comprises two sections, spinning mills and composite mills. There are 103 spinning mills and 275 composite mills, doing both spinning and weaving. In 1960, the total output of the industry was 5018 million yards of cloth (as compared to 3975 million yards in 1936-37 and 4319 million yards in 1948) and 1716 million pounds of yarn (as compared to 1447 million pounds in 1948).

Structure: In the earlier stages of development the industry was confined mainly to spinning, and depended on the China market for the export of yarn. Later it turned increasingly to expanding the weaving section. Here also the industry produced in the early stages only coarse varieties of cloth, the finer varieties being mainly imported or manufactured by handlooms. The years between the two world wars witnessed a large expansion in the manufacture of cloth of fine and superfine varieties. In 1938-39 457 million yards of dhotis and 64 million yards of cambrics and lawns were manufactured as against

169 million yards and 2 million yards in 1927-28. Another noticeable trend is the expansion in the volume of exports of cotton goods. India's exports of cotton cloth increased from 7 p.c. in 1913 to 16·5 p.c. of her total production in 1956. Consequently the country to-day is in a position to depend on domestic sources for meeting almost its entire needs for cloth and also to export substantial quantities to other countries. After taking into account the estimated production of 1200 million yards of handloom cloth, the total output of cotton cloth came to about 15 yards per person.

The industry is spread all over India, though there is some amount of concentration in Bombay area. Over 60 p.c. of the spindles and looms are concentrated in Bombay, and Ahmedabad and the rest being distributed largely in south Madras, Madhya Pradesh, Uttar Pradesh, West Bengal etc. Of the total number of mills (523 in 1961) there are 72 mills in Ahmedabad, 63 mills in Bombay city and 37 mills in the rest of Maharastra, and 40 mills in the rest of Guzarat. Madras contains 139 mills, Uttar Pradesh 29 mills, West Bengal 40 mills etc. There has been a tendency for the industry to move away from Bombay-Ahmedabad to other consuming centres.

The size of mills also varies widely, some of them containing 100.000 spindles, while there are others with less than 10.000 spindles. There are also composite mills with more than 2,000 looms while there are others with less than 200 looms. According to the Report of the Post-war Planning Committee, a composite mill of 25,000 spindles and 600 looms is to be regarded as an economic unit under Indian conditions. In general, the average size of mills is larger in Bombay and Ahmedabad than that in the rest of India.

The industry is almost entirely privately owned and developed mainly by Indian capital and enterprise.

Protection to the Industry: Though the industry began to develop after 1854, it applied for the grant of protection in 1926. The Tariff Board which examined the case for the grant of protection agreed on the necessity of protection, but differed as to the method and extent of protection. Two members recommended a subsidy on yarn and an increase in the import duty on cotton cloth by 4 p.c. The President of the Board did not favour the grant of subsidy, and recommended an increase in import duty by 4 p.c. on both cotton cloth and yarn.

The government did not agree to either suggestion. But as the position of the industry became highly critical, the government had to levy a duty of 1½ as per lb or 5 p.c. *ad valorem* (whichever was higher) on all imported yarn. Since then four Tariff Boards enquired into the position of the industry from time to time. In 1947, protection has been finally withdrawn from the industry. At the present moment, however, imports of all types of cloth and yarn except some special kinds have been prohibited under import control regulations.

Problems of the industry : The most important problem before this industry is the shortage of raw cotton. After the partition of the country, large cotton-growing areas fell within Pakistan. Strained political and economic relations led to a considerable fall in the imports of raw cotton from Pakistan, and the industry had to pass through a crisis in 1950 as a consequence of the shortage in the supply of raw cotton. Since then attempts have been made to increase the domestic production of raw cotton. The First Five Year Plan has provided for increasing cotton production from 2·97 million bales in 1950-51 to 4·23 million bales in 1955-56. This target has been achieved, and now only a small amount of imports would be needed to meet the requirements of this industry.

A second problem is the existence of uneconomic units in the industry and the comparatively low productivity of labour in our country. Quite a number of units are clearly of an uneconomic size, and this means higher cost of production. Moreover, according to the Tariff Board of 1932, the labour cost per lb of yarn in a Bombay mill exceeded that in a Japanese mill by 60 p.c. while the labour cost per loom per day for plain grey cloth in a Bombay mill was over 3 times the cost in a Japanese mill. It is doubtful how far the efficiency of the Indian industry has increased since that year.

Another direction in which considerable improvement is essential is the replacement of plant and machinery. The industry is at present working with plant and machinery most of which was not only but completely outmoded. Nearly 90 p.c. of the machinery in the Bombay mills was more than 25 years old. Operation with such old equipment caused the costs to rise and quality to fall. But the main difficulty in this connection is on the question of finance. It has been estimated that at present prices about Rs. 100 crores would be needed in Bombay

mills alone for modernisation of plant and equipment. The reserves available in the mills are inadequate for this purpose, and the Working Party on this industry has recommended that the government should assist the industry by granting loans at 4 p.c.

Research is another aspect which has not received proper attention at the hands of the industry. The need for conducting research for improving technique and reducing costs in a highly competitive industry like the cotton textile industry requires no special emphasis.

Jute industry : Like the cotton textile industry, jute goods were manufactured in cottage industries in ancient India. As late as the middle of the 19th century the handloom industry was in a flourishing condition. But with the rise of the mill industry. handlooms have disappeared entirely.

The first jute mill was started at Rishra near Serampore by a Scotch gentleman, Mr. George Ackland. The first power loom was installed in 1859. Within a few years, the industry began to make rapid progress. The number of looms increased from 6100 in 1885 to 15335 in 1910, and to 58.639 in 1930.

This industry certainly occupies very prominent place in the economy of the country. The value of fixed capital invested in the industry has been estimated to amount to Rs. 41·2 crores. It provides employment to 2,73.728 workers. Essentially an export industry, it provides the largest source of the country's foreign exchange. One item of its many products, hessian, provides more than 50 p.c. of the aggregate dollar earnings of this country. There are at present 112 jute mills with a total number of 72.161 looms. The total output of jute goods was estimated to be 10·06 lakh tons in 1961 and more than 86 p.c. of the total output was exported in 1961. This is one of the best organised industries of India, having one of the strongest employer's organisation, the Indian Jute Mills Association.

Problems of the industry : Before the World War II, the jute industry suffered from two problems,—that of excess capacity and secondly, the danger of substitutes. The partition of the country has created the problem regarding the supply of raw materials. Lastly, the equipment in the industry is extremely old and there is an urgent need for modernisation of plant and equipment.

One outstanding feature of the industry was the fact that its productive capacity outran the increase in demand. To cope with this problem, the Indian Jute Mills Association has followed a policy of restriction of working hours and sealing a percentage of looms so that a part of the equipment was kept idle. In this way the annual output was sought to be kept within limits so that the price of jute manufactures could be kept at reasonable levels. A consequence of this policy was the expansion of this industry in some of the European and South American countries. Secondly, jute bags have, in recent years, been facing increasing competition from substitutes like cloth and paper bags. Moreover, certain commodities which used to be formerly packed in jute bags are now being bulkhandled, particularly in the U.S.A. As a result, some threat to the continued prosperity of the industry is thus evident.

The third problem, the difficulties regarding the supply of raw jute, has been created by the partition of the country. Of the total jute-growing areas only about 25 p.c. remained in Indian territory after partition. Even of the jute grown in these areas, only about 25 p.c. was really of good quality. Immediately after partition it became clear that the industry was going to face serious difficulties in respect of raw jute supplies. The devaluation of the Indian rupee in 1949 and non-devaluation by Pakistan upset the exchange parity and led to a breakdown of the normal trade relations between these two countries. To meet this situation, besides adopting temporary measures, the government carried on propaganda for increasing the cultivation of raw jute, and the area under raw jute increased from 652 thousand acres in 1947-48 to 1951 thousand acres in 1951-52. Production of raw jute has also increased from 1658 thousand bales to 4658 thousand bales during the same period. It has been estimated that to achieve their targets, mills would need about 6·2 million bales of raw jute, and the output would be about 4·5 million bales in 1960-61. The rest would have to be imported from East Bengal.

Lastly, the Indian jute mill industry which has hitherto enjoyed a semi-monopolistic position in the world markets, is now faced with serious competition from foreign mills. A number of countries like Pakistan, South Africa, Brazil, the Philippines and Japan have started to build up a jute mill industry with completely modern equipment. They are often in a position to undersell Indian goods in foreign

markets. So Indian mills are finding it difficult to maintain their foreign markets unless they took steps to modernise their plants and equipment to the desired extent. The need for such rationalisation was recognised by the manufacturers, and a number of mills had already begun to modernise their plant. It was estimated by the Jute Enquiry Commission that in respect of the remaining mills the cost of modernisation would amount to Rs. 40 crores. The Jute Enquiry Commission recommended that the problems connected with the modernisation of plant and machinery in the jute mill industry should receive the highest consideration of the government.

The Jute Commission also recommended that in order to assist and stabilise the industry, the government should appoint a Jute Commissioner, and set up a Jute Board and a Development Council. It would be one of the functions of the Board to indicate from time to time fair prices for raw jute in relation to jute goods, and notify such prices. On the question of self-sufficiency for raw jute, the aim should be relative rather than absolute self-sufficiency. Endeavour should be made to secure intensive cultivation and improvement in the quality of raw jute rather than to offer inducements for jute cultivation on a wider scale. The Commission also recommended the establishment of regulated markets at important centres in the jute-growing areas in each State. The organisation of multi-purpose co-operatives is essential for improving the lot of the jute-grower, and the State government should give all possible help in this direction.

Iron and steel industry : It is one of the ancient industries of India. That the manufacture of iron from ores reached a high state of development will be evident from the existence of the Iron Pillar of Delhi. The first attempt to smelt iron ores on modern methods was made in 1777 when two Europeans established a company at Jheria for that purpose. From that time, several attempts were made all of which became failure for one reason or other. In 1875 the Bengal Iron Company was started near Asansol. After passing through several vicissitudes the company was finally merged in the Indian Iron and Steel Company.

The real beginning of the industry came after the establishment of the Tata Iron and Steel Company in 1907 at Tatanagar in Bihar. The Indian Iron and Steel Company was formed next year and the

Mysore Iron Works at Bhadrawati in 1923, the Steel Corporation of Bengal in 1937 and the government steel works in Rourkela (Orissa) in 1953. Recently the Government of India have started two more works at Durgapur and Bhilai.

India is fortunate in possessing rich iron ores and coal mines in the vicinity. Iron ores exist in Bihar, Orissa, Mysore and Madras. Some of the richest iron ores in the world exist in the iron belt of the Singhbhum area and these ores contain 55 to 70 p.c. iron. Ample supplies of coal are available in the neighbourhood and other raw materials like limestone, dolomite etc. are also to be found nearby.

The Tatas own iron mines, limestone quarries, magnesite deposits, and coal mines and is therefore, able to reap the advantages of integration. The Mysore Iron Works has been developed by State enterprise, and possesses the only charcoal blast furnace in the world. The total capital invested in the industry has been estimated at about Rs. 61 crores and it provides employment for more than 6 lakh workers. The average wages paid to its workers are the highest in the country. This was the first industry to receive protection in 1924, which was finally withdrawn in 1947. The industry thus enjoyed protection for 23 years and has amply justified the grant of such protection. The total capacity of the main producers for pig iron and steel is estimated to be 1,878,000 and 1,050,000 tons per year. The annual production of pig iron amounted to 41·62 lakh tons in 1960 and that of steel 22·15 lakhs tons in 1960. In spite of this increased production, the country has to depend on imports of steel. It has been estimated that the total demand for steel is about 3 million tons.

The establishment of the steel industry has also fostered the growth of subsidiary industries. Important among these are the tin-plate industry, the wire and wirenails industry, Tatanagar Foundry, Agrico factory and the Locomotive manufacturing industry etc.

Problems of the industry : There is much scope for the expansion of this industry. We possess plentiful supplies of the more important raw materials and the internal demand is growing. Economic development would be hindered if the supplies of iron and steel do not keep pace. The major problem hindering progress in the industry is the lack of finance. To meet this problem, the government has advanced

several crores of rupees to both the Tisco and the IISCO to enable them to carry out expansion and modernisation of their equipment.

A second problem, from long-term point of view, is the inadequate reserves of metallurgical coal. It is well-known that the supplies of high-grade coal would prove insufficient at the present rate of consumption. There are two ways to solve this difficulty :—first, by the adoption of a suitable policy of conservation of metallurgical coal, and secondly, by the adoption of the Krupp-Renn process which uses low grade coal in the manufacture of pig iron.

Coal industry : Coal is one of the basic industries as it is an important source of power. Though coal was known in ancient times, its mining on modern methods may be traced to the year 1774 when the first coal mine was opened at Sitarampore. At that time the chief use of coal was in fusing metals in the arsenals of the E.I. Co. The real growth of this industry came after 1850 when the construction of railways increased the internal demand for coal. The output of coal rose to 21650 tons in 1858 and to 50,000 in 1868. Since then output nearly doubled in every ten years and by 1912 production reached the figure of 12 million tons. The industry had to face certain difficulties after the World War I and in 1924 it applied to the government for the grant of protection. But the government set up an expert committee and on its recommendations passed the Coal Grading Board Act. A Coal Grading Board was set up for the purpose of certifying the grade of coal. In 1926 a Tariff Board was appointed to examine the question of the grant of protection to this industry. The members of the Tariff Board differed in their opinion and the government decided to postpone taking any action. The next important event was the passing of the Coal Mines Stowing Board Act in 1939.

The main coal fields are the Raneegunge field in West Bengal, the Jherria field in Bihar, the Bakuro and Karanpura field in the Pench Valley (Andhra) and other fields in Assam, Kashmir and Bikanir. The known coal reserves are of the order of 43,924 million tons, of which 55 p.c. are in West Bengal and Bihar, 25 are in Madhya Pradesh and 20 p.c. in other States. Total annual production now amounts to 46 million tons (as compared to about 190 million tons produced in Great Britain), of which West Bengal and Bihar produce about 82 p.c. Total investment in the industry is estimated to amount to Rs. 12 crores and it employs about 2 lakh workers.

Problems of the industry: The first problem is the extremely small size of the average coal mine in India as compared to the average size of a mine in the U.K., U.S.A., or Germany. The average output per mine is estimated to amount to 38,000 tons as against an average output of 1 million tons in the U.S.A. There are units producing less than 10,000 tons a year. Such a small size results in uneconomic working of mines and in small financial resources which are retarding the mechanisation and the adoption of other improvements. Lack of mechanisation has been responsible for extremely low output and high cost of production. In Germany less than 2 p.c. of the total production of coal was cut by machines in 1913. In 1928 about 90 p.c. was so produced. As a result the average output per worker increased by 39 p.c. during this period and the price of coal fell by 7 p.c. In India only 424 coal cutting machines were in use in 1951 and they produced only 19 p.c. of the total output. Very little progress has also been made in the mechanical loading of coal. As a result, the output per worker is the lowest in India, being 131 tons per worker against 707 tons in the U.S.A. and 444 tons in South Africa. The small size of the mines with their low output has been an important factor in causing shortage in wagon supply.

The second problem is the conservation of coal resources. It is well-known that our reserves of metallurgical coal are inadequate, especially if the steel industry is to be developed further. Moreover, of the total production of metallurgical coal, about 50 p.c. are being wastefully used in railways, industries and collieries themselves. If the future of the iron and steel industry is to be assured, it is necessary to conserve metallurgical coal. The use of such coal for non-essential purposes is to be banned and the annual output is also to be restricted. The necessity for such conservation is admitted and the recently appointed Coal Board has adopted a number of measures for the conservation of metallurgical coal. The Coal Board has finally laid it down that the production of such coal should be restricted to 7·9 million tons. Besides, coal mines are being encouraged to adopt sand stowing in the mines which would prevent the waste of coal in pillars to support the ceiling. Secondly, steps are being taken to adopt methods of coal washing, which would improve the quality of inferior coal and make it fit for metallurgical and other uses.

There are other problems faced by this industry, *e.g.*, the problem of inadequte supplies of wagons and transport facilities, the problem of ensuring sufficient supply of labour, lack of an efficient marketing organisation etc.

Among possible lines of reform, mention should be made of the demand for the nationalisation of this industry. One of the most important defects of this industry is the extremely small size of the average coal mine. Unless the average size is made considerably larger, there is no possibility of the adoption of improvements like mechanisation, etc. The small units should be amalgamated into large ones. This is not easy of achievement on a voluntary basis under private management. Hence it is necessary that the State should acquire these mines and reorganise them into economic sizes. Moreover, such nationalisation is also necessary to secure the proper conservation of coal resources.

There are also some difficulties in connection with nationalisation. It would require large financial resources, which we lack at present, and it may be questioned how far it would be proper to utilise our limited financial resources in acquiring an existing industry, instead of devoting them to the task of developing new industries. Secondly, we lack technical experts and the proper administrative machinery for the efficient conduct of such a vital industry.

Sugar industry : The sugar industry is one of the major industries of our country. India is the original home of sugarcane and had a flourishing sugar manufacturing industry in ancient times. The real growth of the industry in modern periods came after 1931 when it was granted protection by the government after an enquiry by the Tariff Board. Since then the development of the industry has been very rapid. The number of sugar factories increased from only 32 in 1931-32 to 137 in 1935-36, and production increased from 158 thousand tons to nearly one million tons during the same period. In course of five years India jumped from the 5th to the 1st place among the sugar producing countries of the world. In 1959-60, sugar output amounted to 2·4 million tons.

This industry is important from many points of view, besides making the country self-sufficient in respect of sugar. It has a considerable influence on the rural economy, especially in Bihar and U.P.,

which account for more than 75 p.c. of the total production of sugar in the country. It provides valuable bye-products, which can serve as raw materials for other industries like power alcohol, paper and paper board, straw board etc. About Rs. 60 crores worth of capital have been invested in the industry, providing employment for about 1·35 lakh workers. At the present moment there are about 160 sugar factories of which 72 and 30 factories are in U.P. and Bihar respectively. Madras and Maharashtra possess 16 and 15 mills. The industry has been subjected to close State control almost from the very beginning. In 1934 the government passed the Sugarcane Act and authorised the State Governments to fix the price of sugarcane. In 1937-38, the Bihar and the U.P. Governments passed the Sugar Factories Control Act under which, first, a Joint Sugar Control Board, and later a Joint Sugar Commission was set up to be the final authority on all matters connected with the production and sale of sugar and other matters regarding cane prices. A limited quantity of sugar is also produced in *Khandsaris, i.e.,* cottage or small-scale industries. The grant of protection to the industry was withdrawn in 1950 and the import of foreign sugar is now regulated by the government under import control regulations. The industry has enjoyed protection for an aggregate period of 18 years.

Problems of the industry : In spite of the progress achieved by the industry, there are certain aspects which must raise a sense of uneasiness. As the last Tariff Board pointed out that it was advocating the withdrawal of protection not because the industry could now stand without protection, but because protection had produced an attitude of deplorable complacency on the part of all parties. Though some improvement in efficiency has been achieved, much still remains to be done. The deplorable thing is that not much has been done to reduce seriously the cost of production of sugar. For example, the average yield of sugarcane at first improved from 12·3 tons per acre in 1930-31 to 15·6 tons in 1936-37. After that it has declined. The same thing may be said about the recovery percentage of juice from cane. It improved from 8·66 per cent in 1932-33 to 9·45 p.c. in 1939-40. The maximum so far reached was 10·28 p.c. in 1942-43. But after that year it has dropped to 9·78 p.c. in 1951-52. This should be compared with the recovery percentage of 12·33 p.c. in Cuba, 12·05 p.c. in Formosa and 14·22 p.c. in Queensland. Not much has also been done with regard to the utilisation of bye-products.

The cost of sugarcane forms about 62 p.c. of the total cost of sugar. Hence the industry would not be able to produce at lower cost unless the cost of the raw material is reduced. Reduction in the cost of sugarcane depends on three factors, *viz.*, the yield of sugarcane, the quality of sugarcane, and the early transport of cane to the factories in a fit condition. Increase in the average yield, cultivation of improved varieties of cane and quick transport arrangements, these are essential if the cost of sugarcane is to be reduced. Next in importance is the shorter duration of the crushing season in India as compared to the other sugar-producing countries. The average duration of the crushing season is about 4 to 5 months as against 8 to 10 months in Cuba and Java. The shorter duration in India is due partly to the weather conditions and partly to the absence of early ripening and late growing varieties of sugarcane. If better quality cane is grown and transported quickly to the factories, and if the crushing season can be increased, the recovery percentage can be improved materially with a consequent reduction in the cost of production of sugar. The problem is largely agricultural and much will depend on the extent to which agricultural improvements are adopted.

Next in importance is the question of utilisation of the bye-products of the industry. Bagasse and molasses are the two most important bye-product of this industry. Bagasse can be utilised in the manufacture of packing paper, paper and paper board, cellulose and artificial silk etc. Molasses can be utilised in the manufacture of power alcohol, fertilisers, potash and edible sugar syrups. The quantity of molasses produced every year amounts to about 4 lakh tons, out of which 25 million gallons of power alcohol can be manufactured. This can be used as a substitute for petrol, thereby resulting in a substantial saving of foreign exchange. At present, only 25 p.c. of molasses is utilised in the manufacture of power alcohol.

One of the main problems facing the industry is the inadequacy of cane-supply. The government fixed the price of sugarcane supplied to the factories, leaving it uncontrolled in the case of *gur* production. This has often resulted in *gur* production to increase at the cost of sugar production. Moreover, on account of competition between the *gur* and sugar industries some of the sugar factories have been obliged to start early crushing, utilising unripe cane with the consequent increase in cost of production. Lack of planning the cultivation of early,

medium and late ripening varieties has also resulted in the absence of adequate supplies of cane throughout a reasonably long season. Lastly, the desire of the State governments to wrest a large percentage of the profits of the industry for the cane growers has been followed by the fixation of very high prices for sugarcane. The industry claims that the payment of such high cane prices is responsible for the high cost of production of sugar. Recently the Central Government held a conference for evolving a satisfactory formula for fixing cane prices. The so-called "sisma" formula under which the price of sugarcane is to be fixed not only on the basis of weight but also by taking into account the sucrose content of the cane is now under the consideration of the government.

Tea industry : The tea industry is one of the biggest organised industries of India, and is of special importance to Assam, where about 10 p.c. of the population live in the tea gardens. India is the largest producer of tea in the world and supplies about 40 p.c. of the world's demand for tea. About Rs. 113·06 crores have been invested in this industry, of which Rs. 40·51 crores are Indian (35·8 p.c.) and the rest are non-Indian. and it is the biggest employer of labour, employing more than 10 lakh workers. It is one of the most important export industries of the country, and about 68 p.c. of the total estimated production of tea is exported from India. The value of exports amounted to Rs. 126·39 crores in 1959. The average annual production of tea is estimated at about seven hundred million pounds.

The birth of the industry may be traced to the year 1828 when one Major Robert Bruce discovered the indigenous tea plants of Assam. In 1833 the government made its first attempt to cultivate tea by establishing an experimental tea garden at Lakhimpore in Assam. In 1938 the first consignment of tea was exported to London and in the next year, the government tea gardens were handed over to the Assam Company, the first Tea Company in India. Since then the development of the industry has been very rapid. This was the first industry to feel the impact of British capital, which is still now dominant in the industry. About 60 p.c. of the total acreage under tea is owned by British companies, and of these, about 80 p.c. is controlled and operated by 10 managing agency firms of Calcutta. Another interesting feature is that the marketing of tea in Calcutta is controlled by 3 or

4 leading European firms, and the distribution of tea in the British markets, India's largest customer, is controlled by a small number of firms in the Mincing Lane.

Location. Among the States, Assam occupies the first place. It has 53 p.c. of the total acreage under tea in India and employs over half a million workers. Majority of these gardens are European-owned, Indians owning about 15 p.c. of the total acreage under tea in Assam. Next place is occupied by West Bengal, having 24 p.c. of the total acreage under tea, and employing over 2 lakh workers. South India contains 19 p.c. of the total acreage followed by Punjab, U.P. and Bihar, the last three containing only a small acreage under tea.

Structure. The tea industry combines both agricultural and manufacturing operations. The tea estates generally comprise large areas and belong mostly to joint-stock companies, though there are a number of privately owned gardens. The average size of an Indian garden is much smaller, being about 100 acres, than that of European-owned garden which comprise about 800 acres. Thirteen leading agency houses control about 75 p.c. of the tea production in North India.

The tea industry is remarkable from two points of view. First, it has successfully operated a Tea Control Scheme, aided considerably by government legislation. When the industry felt the impact of the world trade depression in the thirties, the producers of the tea industry in the leading countries met together and adopted a scheme for controlling the exports and production of tea with a view to raise tea prices. The scheme was given effect to through an Act passed by the Government of India. The control scheme succeeded and tea prices rose within a short time.

Secondly, no other industry in India possesses such a bad name for its treatment of labour. There were many abuses in connection with the method of recruitment of labour and the government was forced, from time to time since 1863, to pass laws for the regulation of labour conditions in this industry.

Consumption. Though India produces a large quantity of tea, her annual consumption is comparatively small. Less than one-third of a pound of tea is consumed per person in India, against 9·4 lbs in Great Britain, 7·7 lbs in the Eire and 7·0 lbs in Australia. Great Britain is the largest customer of Indian tea. Efforts are being made

to popularise the consumption of tea in the U.S.A. In order to popularise the consumption of tea in India and in the export markets, the government has set up a Central Tea Board, and levied a small cess on tea. The proceeds of this cess are utilised by the Board in various ways to popularise tea.

The tea industry fell into difficulties in 1952-53, following the decontrol of tea in Great Britain and the consequent cessation of the bulk purchase of tea by the British Ministry of Food. The prices of tea fell considerably even below the cost of production of many firms. The government and the Reserve Bank promptly adopted a number of measures like the postponement of the implementation of the Minimum Wages Act in this industry, special credit facilities to banks lending to tea gardens etc. Fortunately demand for tea revived within a short period of time, and tea prices have risen as a consequence.

Paper industry : The hand-made paper industry was an ancient industry in India. But it has declined substantially in the last century, though of late efforts are being made to revive this section of the industry. The first paper mill was started in 1867 at Bally in Hooghly. A second mill was started in 1882, and since then a number of mills were established all over India. The industry applied for the grant of protection in 1924. It received protection in 1925, which was renewed in different forms till 1947, when it was finally withdrawn. It has made considerable progress under protection. The number of mills increased from 9 in 1925-26 to 16 in 1948 ; the total paid-up capital increased from only Rs. 95 lakhs to Rs. 2·25 crores. At present the productive capacity in the industry has been estimated at 3,21,000 tons and the existing mills are now in a position to meet the demand for writing and printing paper in the country.

The industry is divided into five sections *viz.*, printing, writing, newsprinting, packing and wrapping, and other sorts. Protection was granted only to the first two sections, which have developed as a consequence. The last war gave a great impetus to this industry and many new lines of production have been taken up. At present production covers such varieties as the manufacture of craft and boards like duplex and triplex boards, straw boards, tissue, air mail, bankpaper, bond, ledger paper and cartridges etc. The manufacture of newsprint started in January 1955. India now produces about 22,411 tons of newsprint annually.

The industry is mainly located in West Bengal with an annual rated capacity of 58.500 tons out of a total of 1.36,600 tons. Next in importance comes Orissa with a rated capacity of 3,500 tons and Bihar.

The more important raw materials are bamboo and *sabai* grass. The board industry uses straw, grass and bagasse as the principal raw materials. The main problem before the industry is the shortage of raw materials, which has been accentuated to some extent by the partition of the country. The factories in West Bengal have been deprived of their supplies of bamboo previously obtained from East Bengal. Measures are being adopted for plantation of bamboo and for the development of *sabai* grass in U.P. and Punjab. The collection of waste paper, rags etc., should be more efficiently organised so that these subsidiary raw materials would also become available to an increasing extent. The Planning Commission has recommended the adoption of the following measures to improve supplies of raw materials :—(*a*) Reservation of specific forest areas and the grant of long-term bases for working such areas ; (b) price-fixation on an All-India basis for bamboo and grass to enable the industry to obtain regular supplies at reasonable prices ; (*c*) development of roads in forest areas for facilitating transport ; and (*d*) regulation of exports of waste paper, hessian and jute cuttings, cloth cuttings etc.

The Planning Commission recommended that steps should be taken to increase the number of mills to 19, and the annual rated capacity from 1.36 600 tons to 2,11,000 tons in the paper and paper board industry, an increase in the number of factories manufacturing straw-boards and other boards to 20. In 1960-61 output has been estimated at 320.000 tons. A plant for the manufacture of newsprint has also been set up with an annual rated capacity of 4.200 tons. It is expected to be 60.000 tons by the end of 1960-61.

Other industries : In addition. a large number of other industries like the cement industry. glass industry. match industry. aluminium industry. soap industry, chemical industries like the manufacture of heavy chemicals. paints and varnishes, fertilisers. electrical engineering industries etc.. have been established. The Planning Commission has framed plans for 51 industries.

The government has also established a number of industrial concerns, such as the Sindri Fertilizer Factory, Chittaranjan Locomotive Factory, The Machine Tools Factory, The Hindusthan Ship-building yard and the Hindusthan Steel Ltd., at Rourkela in Orissa. The Sindri Fertiliser Factory contains one of the most modern fertiliser producing plants and is capable of producing 350,000 tons of ammonium sulphate a year. The Chittaranjan Locomotive Factory has already started producing locomotives for the use of railways. The Machine Tools Factory specialises in the production of high precision tools, thus providing a basis for the development of other engineering industries.

Review of industrial development (1850-1950): The real growth of the majority of modern industries in India can be stated to have begun after 1850. So our industrial development is more than a century old. In course of this century, India has succeeded in developing a large number of industries like the cotton textile industry, the jute industry, coal, iron and steel, sugar, matches, paper, cement, glass etc. In view of the total volume and variety of output of manufactured goods, India secured a place among the first 10 leading industrial countries of the world even before the Second World War. That war has given a stimulus to the development of many new industries and to the expansion of existing ones.

In spite of this impressive progress, it must be admitted that by the middle of the present century industrial development had not been commensurate with the size or the resources of this country. This can be illustrated by reference to a number of criteria. It has been stated that one important index of industrialisation is the consumption of steel and heavy chemicals in a country. Per capita consumption of steel is only 8 lbs per year in India against 470 lbs. in Australia, 520 lbs in Great Britain and 360 lbs. in the U.S.A. Per capita consumption of sulphuric acid is 400 times lower in India than that of the U.S.A., and that of soda ash is 100 times lower. Barely 2 p.c. of the working population of the country is employed in large-scale industries. The rate of urbanisation, another index of industrial development, is extremely slow in India, showing that India has yet to experience an industrial revolution on a scale to be found in Great Britain in the 19th century.

Another characteristic has been that industrial development of this century had proceeded at an extremely uneven pace in divergent

directions. There were notable deficiencies in the Indian industrial structure. Only a few heavy capital goods industries were properly developed. Industries manufacturing machineries and machine tools, or those using non-ferrous metals, electrical engineering, automobiles and tractors, prime movers and heavy chemicals were some of the basic industries which were either absent or inadequately developed.

Factors hindering industrial development : What are the reasons for such a slow and lop-sided development of industries in India? A large number of factors such as inadequate supply of capital, which is again shy, dearth of men possessing the pioneering spirit, lack of skilled labour, have been mentioned by writers. A poor country like India does of course, suffer from shortage of capital and of skilled labour. These are well-known handicaps and are to be found in all under-developed countries. Transport facilities were inadequate and the transport policy was also defective. It has often been urged that schedules of railway rates charged in different railways have tended to discourage the development of industries in inland centres, and have actually favoured large-scale import of foreign goods and export of raw materials. The social atmosphere of the country was also to blame to a large extent. It discouraged large accumulations of capital, and the conservative atmosphere in the joint familes killed initiative and enterprise in many a young man. The high esteem placed on Government service attracted the best talents of the country. The result was the dearth of really able men to develop the industries.

Several reasons have been advanced by the Indian industrialists to explain the slow rate of development of the industries. Before 1947, the main factor hindering industrialisation was the policy pursued by the government regarding the grant of protection. The policy of discriminating protection was adopted only from 1924. Before that year the Indian industrialists were unable to face the cut-throat competition of well-established foreign concerns. After 1924 the government no doubt adopted the policy of protection. But it was applied very haltingly, and investors and industrialists could not be sure of getting adequate protection from the government. After 1947 the position changed for the better with the advent of independence. But there have been two other factors sapping the confidence of the industrialists. One is the heavv rates of taxation levied bv the government which do not leave adequate incentive for the development of new industries.

Secondly, the labour policy pursued by the government since 1947 is an important factor making for the slow rate of development of industries. It has been urged that the labour policy of the present government is resulting in high labour cost, low output and considerable indiscipline among the workers.

The last two points have been much exaggerated. In every country efforts to introduce humane conditions of work for labour have not always been looked upon with good grace by the employers. The charge that the burden of taxation is crushing is also to be very frequently found in every decade. Income-tax at the rate of 25P. per rupee was looked upon by the early generations as the limit. The present generation would sigh with relief if the rate of tax is lowered to 50P. per rupee. It must, however, be recognised that the reactions of businessmen and investors are not always governed by rational considerations, and as Keynes stated in his *General Theory* that "in estimating the prospects of investment, we must have regard, therefore, to the nerves and hysteria and even the digestions and reactions to the weather of those upon whose spontaneous activity it largely depends."

Industrial Development during the three Plans : The years of planning since 1950-51 have witnessed a remarkable development of industries in the country. There have been important changes in the rate of growth in industrial output and in the pattern of industrial growth. During 15 years the general index number of industrial production had recorded a cumulative rate of increase by about 7 p.c. per year. The actual increase had, moreover, been probably much larger, as a number of new industries had been established during the latter part of this decade and these had not been included in the index number.

There have also been large changes in the pattern of industrial development. Upto 1950, it would not have been wrong to state that with the exception of the coal and the iron and steel industry, no other basic industry had been developed, and the industries that had been established so far consisted mainly of consumer goods industry. But during the Second Plan period greater attention had been paid to the establishment of a number of basic industries, *e.g.*, metallurgical, mechanical and electrical engineering and chemical industries. Most of

this development had been undertaken by the State, which invested something like 974 crores of rupees in the development of key industries and minerals. Three new steel plants have already been set up in the public sector and the two plants in the private sectors had been aided by the state to expand their output. Significant expansion had been secured in the production of essential industrial materials like aluminium, cement, heavy chemicals and dyestaffs, fuel such as coal and petroleum and of power.

Steps had also been taken to secure the rapid growth of machine-building industries. The value of machine tools produced in India increased from Rs. 34 lakhs in 1950-51 to Rs. 550 lakhs in 1960-61, and this country is now producing increasing quantities of machinery for use in agriculture, transport, textiles, Jute, Cement, Tea, Sugar, flour and oil mills, paper, mining chemicals and pharmaceuticals etc. A heavy machine-building, plant and a foundry forge plant had been set up at Ranchi, a coal-mining machinery plant at Durgapur and the Heavy Electrical Project at Bhopal had also been established.

A growing number of new industrial items *e.g.*, industrial boilers, milling machines and other types of machine tools, tractors, industrial explosive, sulpha and antibiotic drugs, D.D.T. newsprint, motor-cycles and scooters, dyestuffs, staple fibres etc. Rapid progress had also been achieved in industries manufacturing durable goods such as automobiles, fans, radios, electric lamps, sewing machines etc.

Thus it would be no exaggeration to state that the pace of industrial development achieved during the last decade had been such as to lay good foundation for a highly developed, self-reliant industrial economy. It will not be wrong to say that India is now passing through an industrial revolution in course of the second and the third plans.

Questions

1. Give a brief history of the growth and state the present position of the cotton textile industry in India. What problems are being faced by the industry at present ?

What problems have faced the Indian cotton mill industry since the end of World War II ? What measures would you suggest to improve the present position of the industry ? (C. U. 1961).

2. Consider the present position and future prospects of the Jute Industry in India.

3. Give a short account of the Iron and Steel Industry in India. What steps are being taken by the Government to develop it and increase its targets of production ?

4. Give an account of the Indian Sugar Industry, indicating the factors that promoted its growth.

5. Describe the factors hindering the growth of large-scale industries in India.

"The industrial system in India is unevenly and in most cases inadequately developed." How do you account for this ?

6. Write a lucid note on the industrial development of India during the past decade.

7. By what criteria should India be classed among undeveloped areas ? On the light of your answer how do you explain the high ranking that India enjoys among the industrial countries of the world ? (I.A.S. 1955)

CHAPTER 22

INDUSTRIAL MANAGEMENT AND FINANCING

As in other countries the majority of large-scale industries run by private enterprise are operated by joint-stock companies. A most important characteristic of these companies is that they have been almost invariably organised under firms known as the managing agents. What are the features of this system, and how far has it fostered or hindered the industrial development of this country ? It will be our next business to examine this very important question.

Managing agency system : The managing agency system is a peculiar feature of the industrial organisation of India. A managing agent is a firm which is entrusted with the task of managing an industrial concern under an agreement with the parent company, subject to the directions of the Board of Directors. Though the system is peculiar to India, it is not an indigeneous institution. It arose as the outcome of British trade relations with India. When the British capitalists began to invest capital in developing industries in India, they had to face one difficulty,—how to find, among the relatively small number of foreigners living in India, persons who could manage their concerns ? The agency houses, formed by the ex-servants of the East India Company, took up this task and began to manage everything, including the supply of finance. The latter function was rendered easier on account of the fact that they were at that time acting as bankers. Hence they came to be known as managing agents. In course of time they began to float industrial concerns on their own responsibility, appointing themselves as managing agents. As the advantages of the system became apparent, it tended to become universal, and the Indian industrialists quickly adopted the practice.

Organisation and functions. The managing agency firms have been organised in four different ways,—private firms, partnership, private limited companies and public limited companies. At present there is a tendency towards converting other firms into private or public limited companies.

They perform three types of functions in relation to concerns under their management. First, they pioneer the development of

industries. They organise and start a new concern, float shares for sale in the market, appointing themselves as managing agents. Almost all the important industries like jute, cotton textile, iron and steel, paper, etc., have been organised by different firms of managing agents.

Secondly, they manage the day-to-day affairs of concerns under their control. They purchase raw materials and machineries, arrange for the sale of the products, and appoint the necessary staff.

Lastly, they also supply some finance to the industrial concerns. They buy or take up a portion of the shares or debentures in these concerns or provide long-term loans for financing schemes of extension or re-organisation. They have also supplied a part of the working capital either from their own funds or by guaranteeing loans from banks. Banks have followed the practice of granting loans on the guarantee of the managing agents. It is the good name of the managing agent which has induced investors in Ahmedabad and Bombay to deposit funds with industrial concerns and these deposits are utilised as working capital by these concerns. A number of managing agents have also extended financial aid to their concerns during emergencies or depressions often at serious inconvenience to themselves. Their part in financing industries was, therefore, substantial.

In recent years a number of facts have been published with respect to the activities of the managing agents. In 1954-55, there were about 3944 managing agency firms which controlled about 17 p.c. of the total number of all joint-stock companies. But the companies under the managing agents accounted for nearly half of the total paid-up capital of all companies. The vast majority of these managing agency firms (about 89 p.c.) managed just a single company each. About 401 managing agents controlled 2 to 9 companies each while 17 large managing agencies managed 10 or more companies.

Regarding the extent of their participation in financing the concerns under their management, the practice varied in different regions. Prof. S. K. Basu found that in Calcutta, the managing agents held about 13·58 p.c. of the total paid-up capital of the companies managed by them. The average holding of the European managing agency houses was 10·11 p.c., while it was as high as 42·4 p.c. for Indian managing agencies. The average holding varied from industry to industry, the lowest being 5·03 p.c. in the coal industry. The

proportion is higher for managing agents in the western region and everywhere it is rising due to the fear of the take-over of managing agency by rival groups.

Advantages : That the system contributed a great deal to the industrial development of this country may be readily admitted. During the early years of industrialisation they have borne the risks of pioneering and developing industries at a time when the prospects of industrialisation were comparatively unknown. Even at the present it is the managing agent's responsibility to nurse a venture into the profit-earning stage in the early years of a concern's life. Secondly, the managing agents proved to be a tower of strength to industrial concerns during depression or bad times. The guarantee and financial standing of the managing agents have enabled these concerns to obtain loans from the banks on easy terms. Thirdly, the widespread prevalence of this system has resulted in the grouping of a number of concerns under unified control and management. This fact yields undoubted advantages in certain directions. When many concerns are under one management, there are obvious economies of buying and selling on a large-scale, secured by all these concerns. There are economies in the cost of maintenance of supervisory and technical staff. The same technical staff of greater ability and experience can be utilised for different concerns, and this is an important advantages in India where there is a dearth of technical talent. On the whole there is no doubt that the system has contributed a great deal to the promotion and financing of sound industrial concerns.

Defects. But one must also remember the important defects of this system. Before 1936, when most of the managing agency firms were organised on a private or partnership basis, the children of the original agent automatically inherited their father's firm. While the father might have possessed great business ability, there was no guarantee that his children would also inherit the same efficiency. As a result, the concerns suffered on the death of the original founder. Secondly, many firms became managing agents because they possessed adequate financial resources. They are usually prone to give greater attention to the financial and commercial aspect of the operation of the concerns under their management, neglecting the technical side. This resulted in lowered efficiency. Thirdly, though the system secures some benefits of centralised buying and selling, there was no guarantee that these

benefits would be passed over to the concerns. The resulting benefits have often been pocketed by the agents themselves. Fourthly, as rgards the function of promoting of industrial concerns, it has been stated that many of the agents have been very conservative, imitative and unable to break new ground. Moreover, as there is seldom any co-operation between different managing agencies, the floatation of large enterprises requiring huge amount of capital has become difficult.

But the greatest defect is concerned with the payment of remuneration to the managing agents. Before 1936, the managing agents received their remuneration usually in two forms, *viz.*, a fixed sum on account of office allowance and a percentage on sale of output or profits. As regards the first method of payment, it has been urged that the industrial concerns have not always obtained full value for the expenses as in many cases the amount of office expenses is much in excess of the actual sums spent by the agents. The system of giving the agents a commission on sale or output tended to lead to overproduction as the more is the output or sale, the more is the agent's commission, irrespective of the fact whether the concern earned any profit or not. The interests of the concerns have thus often suffered as a consequence. Moreover, if we consider the different ways in which the agents have made money out of the concerns, it would be evident that they realised too large a share of the profits. The natural consequence of such a situation has been to make investment in industrial shares less attractive to the ordinary investors.

The system has also been criticised on other grounds. The agents have usually a large number of concerns under their management. Many of them invested the surplus funds of one concern in the shares and debentures of others concerns under the same management. Reserves of several well-established mills have been frittered away by lending them to others newly started by the agents. To save weak concerns the agents invested the funds of the stronger ones, and this had often led to the ruin of the latter when the former collapsed. Thus the practice of inter-investment of funds led to grave evils. Moreover, there have been cases where some managing agents traded and speculated rather excessively with the funds of their concerns and the resulting weakness in their position reacted adversely on the financial condition of the concerns under their management. Many of them packed the Boards of Directors

with their nominees and so virtually deprived the shareholders of any effective control over the concerns.

Lastly, it is argued that the system has resulted in an aggregration of industrial power in the hands of a small number of firms and has to that extent a monopolistic and anti-social trend. Dr. M. M. Mehta has shown that among foreign agency firms Andrew Yule and Mcleods control and manage more than 90 concerns; Dalmias control 40 concerns ; J. K. industries 42 concerns ; Thapars 32 concerns and Birlas manage or control more than 2 dozen firms. The system has thus tended to concentrate wealth and economic power in a few hands and modern democratic tendencies have naturally begun to frown upon its continuance

Attempts at reform. In view of the well-known abuses of the managing agency system the government made several attempts to remove some of its worst defects. The first attempt was made in 1936 at the time of the revision of the Indian Companies Act. Amendments to that Act laid down a number of provisions or restrictions on the working of the system. The first was that no managing agent could be appointed with regard to a banking or insurance company. Secondly, no one could be appointed as managing agents of a company for more than 20 years, after which the agreement would have to be renewed at a meeting of the shareholders. Thirdly, to prevent the packing of the Board of Directors with the nominees of the agents, it was laid down that not more than one-third of the total number of Directors could be nominated by the agents. Fourthly, the remuneration of all managing agents appointed after the Act was to consist of a fixed sum of office allowance and a percentage of the net profits of the concerns, unless the shareholders decided otherwise. Thus payment of a commission on sale or output was prohibited in the case of all future managing agents. Fifthly, no agent could employ the funds of a concern in the purchase of shares or debentures of any other company under the same management. The grant of a loan to, or the guaranteeing of loans of, managing agents was also absolutely forbidden. Lastly, the managing agent was debarred from carrying on a competitive business on his own account.

These provisions no doubt sought to do away with some of the worst abuses of the system. But they left many problems unsolved, many criticisms unanswered. For example, the rule that the remuneration of managing agents was henceforth to consist of a percentage of net

profits was qualified by the expressed, "appointed after the Act." As a result, a large number of managing agents appointed before 1936 continued to receive their remuneration in the form of a commission on sale or output. In the meantime there were a few cases when the shares and rights of the managing agency firms were sold in the market, threatening a number of grave evils. This unrestricted transfer of managing agency rights might lead to the transfer of the management of concerns to incompetent or unscrupulous hands, which shareholders would be powerless to prevent. So the government had to intervene and in 1951 an amending legislation was passed under which it was laid down that the transfer of his office by the managing agent would not be valid without the approval of the Central government. In the meantime the government appointed the Company Law Committee under Shri H. Bhaba to suggest reforms of the Indian Companies Act. The Committee issued its report in 1952 and made a number of recommendations for removing the abuses of the managing agency system.

Companies Act of 1956. The recommendations of the Company Law Committee were examined by the government, and a new Companies Act was passed in 1956 to incorporate them. These amendments aimed at the removal of some of the well-known abuses of the managing agency system and at plugging the loopholes of the previous legislation. It also provided for the abolition of the system in certain lines of production. Sec. 324 of the new Companies Act empowered the central government to notify that companies engaged in specified industries or business should not have a managing agent. A second provision was that the term of office of all existing managing agents was to expire on the 15th August, 1960, if it did not expire earlier. In future none could be appointed as a managing agent for more than 15 years in the first instance Any existing agent could be re-appointed for another term which should not exceed 10 years provided that the resolution was passed by the company at its general meeting, subject to the approval of the central government. It was open to the central government to withhold its approval, unless it was satisfied that it was in the public interest to allow the company to have a managing agent, and that the terms of the managing agency agreement were fair and reasonable, and that the managing agent was a fit and proper person. But before vetoing such re-appointment the Central Government would have to consult the Company Law Advisory Commission. It has also been laid

down that after 15th August, 1960, no one can hold office as managing agents in more than 10 companies.

There are also important provisions for regulating the remuneration of the managing agents. The remuneration of a managing agent cannot exceed 10 p.c. of the net profits of the company, subject to a minimum of Rs. 50,000, if, in any year, there are no profits or inadequate profits. The remuneration is not to be paid before the accounts are audited and laid before the general meeting of the company. The payment of additional remuneration beyond 10 p.c. of the net profits may be sanctioned by a special resolution of the shareholders of the company and approved by the Central Government. The overall limit is, however, 11 p.c. of the net profits. The payment of an office allowance is not to be allowed. But he may be re-imbursed in respect of actual expenses incurred by him on behalf of the managed company. A section of the Act prohibits a managing agent from receiving any other sum from the company, whether directly or indirectly, by way of remuneration, rebate, commission, expenses or otherwise.

There are also other restrictions on the operations of the managing agents. No managing agent can henceforth engage on his own account in any business which is of the same nature as, and competes directly, with the business carried on by the managed company under the latter authorises him to do so by a special resolution. The managing agent can appoint only one Director to the Board of Directors of the managed company when the total number of Directors is less than five, and not more than two when the total number of Directors is more than five. There are also important restrictions on the investment of thte funds of one company in another under the managing agent.

The Act also lays down a number of limits to investments which may be made by a company in another company under the same managing agent. Such investments can be made only on the unanimous approval of the Boad of Directors. No company can invest more than 20 p.c. of its subscribed capital in other companies under the same management, nor can such investment exceed 10 p.c. of the subscribed capital of a company in whose shares the investment is made. These limits may be exceeded only if a resolution to that effect is passed by the meeting of the shareholders of the company, and is approved by the Central Government.

There are also other restrictions on the powers of the managing agents. No relation of a managing agent can be appointed to a post in the managed company without the sanction of the Board of Directors of the latter company. Another section prohibits a company from giving a loan to its managing agent except for facilitating the company's business and subject to limits fixed by the Board of Directors and such loans shall not exceed Rs. 20,000 in the aggregate.

These are important restrictions which aim at the prevention of the abuses of the managing agency system. If the provisions of this Act are sympathetically administered, it will enable the system to function within proper limits and to give its best to the task of building up the industries of the country.

Companies (Amendment) Acts, 1960, 1963, 1965 : The Companies Act of 1956 were amended in subsequent years to remove certain defects and deficiencies noticed in its working. These amendments sought to lay down further restrictions on the working of the managing agency system. For example, as the Companies Act of 1956 prohibited the appointment of managing agents as the buying and selling agents of the company, a number of managing agents resigned and appointed themselves as managing directors, and retained its functions as the buying and selling agent of the company. The 1960 amendment provided that in certain industries or commodities notified by the government buying and selling agents can be appointed only with the sanction of the government. More restrictions have been placed on the manner, in which the remuneration of the managing agents is to be calculated. Payment of any remuneration to any partner or a director of the managing agency firm is to be included in calculating the remuneration payable to the managing agent. In 1959, the government passed orders for fixing a sliding scale of commission to be paid to the managing agents by the companies managed by them, the scale varying from 10 p.c. of the first Rs. 10 lakhs of the net profit to 4 p.c. on any sum over Rs. 1 crore. The 1965 amendment has placed more restrictions in respect of inter-company loans. A public company may lend money upto 10 p.c. of its own subscribed capital and free reserves without any special resolution, and upto 20 p.c. to companies under the same management with prior special resolution. But it shall not give loans in excess of these limits without the sanction of the government.

In 1965, the government appointed a committee under the chairmanship of Shri I. G. Patel.

That committee recommended the discontinuance of the managing agency system in these industries, sugar, cotton textiles and cement. Companies belonging to these industries should, however, be granted a reasonable period of time for making the change. The committee did not like the abolition of the system with respect to jute and paper industries as condition in these industries are not yet ripe for such a measure. After the abolition, the companies are to be managed by managing directors. While the long-run policy should be to discourage the system, the committee recommended caution with respect to its immediate abolition in other industries. In the resolution issued by the government on a review of the report of this committee, the government has recommended the abolition of the system in all the five industries mentioned above.

Abolition of the system? In the debate on the Bill in the Parliament a demand was made for the abolition of the system of managing agents. There is much to be said on both sides. The justification of the system lay in the conditions which existed in the early days of industrialisation. But these conditions have changed, while the newer managing agents lack the experience, technical competence and the financial resources of the old agency firms. The old fashioned type of men who have made some money in trade and commerce and gained some knowledge of industry by empirical methods of management are definitely an anachronism under modern conditions. In the opinion of many, it is not possible to remove the evils of the system by means of legislation, however elaborate it may be. Such legislation may easily be evaded, while too many restrictions may result in making the system rigid and inefficient. Hence abolition, not reform, is the proper policy to be followed in this case.

On the other hand the advocates of the system have pointed to the undoubted benefits conferred by it upon the country. It has been claimed on behalf of the system that companies with managing agents have on the whole yielded a far better return to the shareholders, greater production and higher contributions to the revenues of the government in taxation than those without managing agents. The system has not outlived its utility, but should be allowed to continue with necessary adjustments and proper safeguards.

In a recent analysis of "the chained managing agency system". Dr. S. K. Basu has carefully examined the virtues of the system. In his opinion, there is virtually no difference between the efficiency of managing agents and that of the Board of Directors. The managing agents' contribution to the share capital of the concerns under their management is now insignificant. Moreover, the government has now set up a large number of financial organisations for providing funds to the industrial concerns. The task of company promotion is now being undertaken independently of the managing agents. A large number of concerns have been floated very successfully without managing agents. In fact companies promoted by managing agency firms have formed only a small part of the total company floatations in recent years. So he concludes that 'the future of the system in the country will in the ultimate analysis depend on its "good behaviour", and its risilence to the modern dynamic age—on its efficiency, foresight, breadth of outlook and its achievement of a high standard of business morality."*

Financing of industries : It has been one of the well-known complaints that the industrialisation of this country has been hindered for want of adequate finance. It is, therefore, necessary to examine this question at this place. We propose to start by discussing the present sources of supply of finance.

The problem has been studied with reference to cottage and small-scale industries. The problems of large-scale industries are to some extent different, and should be treated separately. We propose to study the financial problems of large-scale industries.

Financing of large-scale industries : An industrial concern needs finance for two purposes, *viz.*, initial finance for the purchase of land, construction of factories and other buildings, installation of machineries etc. A going concern needs finance for carrying out extensions, rennovations, modernisation of plants etc. The sums invested in these ways constitute its block or capital expenditure. Secondly, it requires finance for the purchase of raw materials, for the payment of wages, for marketing and other recurring items of expenditure. This is known as its working capital. To meet their

* Dr. S. K. Basu, *The Managing Agency System—In Prospect and Retrospect*, p. 207.

capital expenditure, concerns need funds for long periods, whereas working capital requirements can be met from short-period funds.

Large-scale industrial concerns have so far attempted to raise their finance from the following sources, *viz.*, sale of shares and debentures among the public, loans from banks, funds supplied by managing agents, deposits from the public, indigenous bankers, and recently, the Industrial Finance Corporation. The government has also granted long-term loans to a few large concerns, *e.g.*, the Tata Iron & Steel Co., the Steel Corporation of Bengal etc.

For a concern organised on the joint-stock principle, the most usual source of finance is through the sale of shares and debentures in the market. In this way funds are raised from the investing public. While some companies have floated debentures with success, these are not usually favoured by our investors on account of a number of factors. As a result, the proportion of debenture capital is very small as compared to the total amount of share capital. Shares are now-a-days more popular. But the resources of the Indian money market are comparatively limited in view of the fact that the total volume of savings in this country is very small. Moreover, some of the savers are very conservative and prefer investment in land and government securities to that in the purchase of industrial shares. As a result, most of the concerns have not been able to raise enough capital by the sale of shares. In the Western countries, companies follow the practice of issuing enough share capital needed to meet the whole of their capital expenditure plus a large part of their working capital, but not so in India.

Loans from banks provide a most important source of supply of finance, especially for working capital. Banks generally supply short-term loans against the security of the stock-in-trade, and often against the guarantee of the managing agents. The industrialists have complained that the volume of loans granted by banks is inadequate, costly and hedged in with many onerous conditions. Banks, in their opinion, are too conservative and seldom advance loans for long periods. Many of these criticisms are of course wrong, and we must remember that banks whose major resources consist of short-term deposits cannot afford to tie up their funds in long-term loans.

The smaller concerns among the large-scale business units sometimes borrow from the indigenous bankers and shroffs. But the latter

generally charge high rates of interest and the burden of fixed interest payments weighs heavily on these concerns.

The industrial concerns also secure a portion of the needed finance from their managing agents. These agents subscribe to the shares and debentures at the time of initial floatation of the companies. Thus they supply a portion of the long-term funds, though they may subsequently sell out their shares and debentures to the public. They also supply some funds to meet the working capital needs, and grant occasional loans to the concerns under their management. They also have to guarantee loans taken by these concerns from banks. Some of the agents have extended financial help to concerns under distress, thereby enabling the latter to survive the crisis. While their services in supplying finance for industrial development are not negligible, it is desirable that in future industrial concerns should try to be independent of the managing agents.

In Bombay and Ahmedabad, the cotton textile industry secured a part of its working capital through public deposits. The mills accept fixed deposits from the public, and about 39 p.c. and 11 p.c. of the funds invested in these concerns were obtained from this source in Ahmedabad and Bombay. One serious defect of this method of finance is that the deposits are liable to be withdrawn by the public in panic during periods of distress when the need for funds is very urgent. Thus reliance on this system of financing is not desirable.

Since the foundation of the Industrial Finance Corporation, larger concerns are getting long-term loans from this institution to enable them to finance extensions and rennovations.

A review of the existig system. We have reviewed all the important sources for the supply of industrial finance for large-scale industries. There is a persistent complaint that these industrial units are hampered on account of the inadequacy of capital. The greatest difficulty is with regard to the supply of long-term capital. In respect of working capital the problem has not proved so acute at least in the case of large-scale units. The inadequacy of long-term capital is due to the small amount of savings available for industrial investment in a poor, underdeveloped country like India, and to a number of other ancillary factors such as adverse economic climate etc., which impede the flow of savings into industries.

Improvements in the system of industrial finance : In view of the complaints regarding the inadequacy of finance for industries, the Reserve Bank of India set up a Committee in 1953 to examine how increased finance could be made available to the private sector. The report of the Committee, known as the Shroff Committee, made a number of recommendations to this effect and we propose to examine them at this stage.

After reviewing the steps taken by the government and the Reserve Bank of India to increase the flow of funds for industrial development, such as the establishment of the Industrial Finance Corporation, the introduction of the Bill Market scheme, investment by the Reserve Bank in the share capital of Industrial Finance Corporations, promotion of sound banking practices etc., the Committee felt that with a number of other suitable adjustments in the Reserve Bank's lending and rediscounting practices, the commercial banks, insurance companies and other financial institutions would be able to make larger investments in private industry.

The Committee rightly emphasized that the scope for direct long-term lending by banks must necessarily be limited in view of the fact that their resources consisted mainly of deposits withdrawable on demand. But banks should adopt a more liberal policy towards increasing their investments in the shares and debentures of first class industrial concerns, making larger advances to approved parties against such securities. They should also subscribe to a greater extent to the shares and bonds of special institutions like the Industrial Finance Corporation and the State Finance Corporations. In order to facilitate the last type of investment the Reserve Bank should treat the shares and bonds of the Financial Corporations as on a part with government securities for purposes of granting advances. Secondly, banks might form a Consortium or Syndicate under the leadership of the Imperial Bank of India, and with the co-operation of insurance companies for the purpose of under-writing or investing in new issues of industrial shares and debentures.

The Committee also made a number of other recommendations for increasing the resources of banks or for enabling them to grant more advances to industrial concerns. In the first place, the Reserve Bank should adopt a series of measures for cheapening and quickening the remittances of funds in the mufassil areas. This would enable

banks to keep smaller cash balances in their branches, thereby enabling them to lend larger sums. Secondly, in the original Bill Market Scheme, the facilities granted by the Reserve Bank (i.e., rediscounting at $\frac{1}{2}$ per cent less than the Bank rate) were restricted to scheduled banks with deposits of Rs. 5 crores or over. The Committee recommended that the facilities should also be extended to all scheduled banks with deposits of Rs. 1 crore or over, and that the minimum amount of such bills eligible for rediscount should be reduced from Rs. 1 lakh to Rs. 50,000 and individual advances from Rs. 25 lakhs to Rs. 10 lakhs. Thirdly, to facilitate the opening of more branches in the rural areas and so to attract more deposits, the Reserve Bank should, in consultation with the government, work out a detailed scheme of financial assistance to banks desirous of opening branches. Moreover, the government should set up an Expert Committee to examine ways and means of rationalising the wages and salary structure in banks so that opening of more branches of banks might not prove onerous on account of high operating costs.

The Committee has also suggested that the indigenous bankers should reform their practices, and organise their banking business properly. Steps should also be taken to encourage the rediscounting of usance bills of indigenous bankers by the Reserve Bank through the scheduled banks.

The insurance companies could also play a more important part in financing industries than they were doing. The Committee recommended that the Insurance Act should be suitably amended to enable these companies to invest up to 5 p.c. of their investible funds in any one company, and to invest in the shares and debentures of industrial concerns to a larger extent than before. The Act should also be amended to reduce the statutory minimum investment in government securities by insurance companies from 50 per cent to 45 per cent.

The Industrial Finance Corporation should also play a greater part in financing industries, and to facilitate this, the Commitee has recommended that (*a*) the IFC should grant debenture-loans, (*b*) it should explore the possibility of converting the whole or part of a loan granted by it into share capital on mutually agreed terms, and (*c*) it should examine the scope for lending jointly with banks or guaranteeing industrial advances granted by banks and industrial companies.

Lastly, the Committee has stressed the need for setting up such institutions as issue houses, investment trusts, unit trusts etc., for mobilising financial resources. It has also approved the proposal to establish the government-sponsored Industrial Development Corporation.

The merit of this Committee is that it has recommended just those things which are the stock-in-trade of almost all writers on this subject.

Industrial Finance Corporation : That the industrial development of India has been hampered through lack of adequate finance has long been stressed. To remedy this defect, the necessity for establishing a specialised institution like an Industrial Bank has been pointed out long ago by the Industrial Commission of 1918. A recommendation to that effect was also made by the Central Banking Enquiry Committee of 1930-31. Before the Second World War, one or two private industrial banks, were organised in India. But on account of a variety of factors almost all of them proved unsuccessful. After the war, the government took up the proposal and passed an Act for setting up an Industrial Finance Corporation (IFC), and it was established in 1948.

The IFC is a semi-autonomous, semi-public institution with a capital of Rs. 10 crores, divided into 20,000 shares of Rs. 5,000 each. These shares have been subscribed by the Central Government, Reserve Bank of India, the scheduled banks, insurance companies, investment trusts and other financial institutions in proportions laid down in the Act. No private individual is entitled to hold shares in this concern. The shares are guaranteed by government with regard to repayment of capital and payment of dividend up to 2½ per cent. The management of the IFC has been entrusted to a Board of Directors, consisting of a Managing Director, appointed by the government on the recommendation of the Board of Directors, three Directors nominated by the government, two by the Reserve Bank and two Directors each to be nominated by the scheduled banks, insurance companies and other shareholders. The Board is to be guided in policy matters by the instructions given by the government.

Besides its paid-up capital, the IFC may accept deposits from the public repayable after not less than five years. The total volume of such deposits is not, however, to exceed Rs. 10 crores. It may also sell bonds or debentures which may be guaranteed by the government as to the repayment of capital and interest. The total value of such bonds

or debentures is not to exceed five times the amount of its paid-up capital and reserves.

The main function of the IFC is to grant medium and long-term loans to large industrial concerns, specially when such concerns are unable to secure funds through normal banking channels or through the issue of shares to the public. The IFC can lend only to public limited companies or to co-operative societies registered in India. It may provide accommodation to these concerns in three ways. First, it may make direct long-term loans or subscribe to the debentures of these companies. Such loans or advances must be repayable within 25 years and the amount of loan to any single borrower must not exceed Rs. 1 crore (it was Rs. 50 lakhs in the original Act). Secondly, it may guarantee the loans to be raised by industrial concerns from the market. Thirdly, it may underwrite the issue of shares or debentures by industrial concerns, subject to the condition that if a part or whole of the underwritten capital remains unsubscribed by the public, these must be disposed of within 7 years. The IFC can also directly subscribe to the shares or stocks of any company.

A recent amendment to the IFC Act has sought to enlarge its resources and scope of functions. The IFC may now borrow from the Reserve Bank of India against government securities for short periods not exceeding 90 days, and also against its own bonds and debentures up to a maximum of Rs. 3 crores and for periods not exceeding 18 months. It may also borrow from the World Bank for financing the foreign exchange requirements of its borrowers and the government has been authorised to guarantee such loans. Thirdly, it may grant loans to shipping companies, and the maximum amount of any single loan was raised from Rs. 50 lakhs to Rs. 1 crore.

Another amendment was passed in 1960-61 to enlarge the scope of the activities of the IFC. It authorises the IFC to guarantee (*a*) loans raised by industrial concerns from the scheduled banks and the State Co-operative Banks, (*b*) deferred payments due from industrial concerns in connection with their purchase of capital goods both within and outside India, and (*c*). with the prior approval of the Union Government , loans raised by industrial concerns in any foreign country. The IFC has also been authorised to subscribe directly to the stock or shares of an industrial concern and also to convert, at its option, loans

granted or debentures subscribed by it, into stocks or shares of the concern.

According to the 13th annual report of the IFC, the Corporation had received 763 applications for loans in thirteen years of its existence, of which it had sanctioned 386 applications for a total amount of Rs. 105·82 crores. Of these 253 applications for Rs. 76·55 crores were in respect of new undertakings. Industry-wise, the largest amount of loans (Rs. 30·27 crores) was granted to sugar industry, followed by paper (Rs. 13·24 crores) and textiles (Rs. 12·15 crores), chemicals (Rs. 10·93 crores), and cement (Rs. 6·67 crores). The Corporation had also sanctioned loans to co-operative factories; as much as Rs. 23·27 crores had been granted to 28 co-operative factories (mostly producing sugar). The Corporation had also undertaken the business of under-writing of shares and debentures and guaranteeing of deferred payments due from industrial concerns in respect of imports of capital goods. It had also issued debentures to the public which had been over-subscribed. The IFC secured its funds by issuing bonds and debentures, and borrowing from the Reserve Bank. It has not taken any deposits from the public.

The IFC secured its funds by issuing bonds and debentures, and borrowing from the Reserve Bank. It has not taken any deposits from the public.

The IFC has come in for a good deal of criticism. First, it has been urged that the IFC takes a long time to sanction a loan and that there is also considerable delay before the sanctioned loan is paid to the borrower. In successive speeches, the Chairmen of the Corporation have tried to answer this criticism. The delay has often been due to the fact that the borrowing concerns do not comply promptly with the conditions regarding the grant of a loan, and that in the last two years attempts have successfully been made to speed up the procedure regarding the grant of loans.

Secondly, though it appears that the IFC has been granting a large proportion of its loans to "new" concerns, *i.e.* those set up after August 15, 1947, it should devote more attention to help new lines of activity, which ordinarily find it difficult to raise sufficient funds from the market. There is no reason why it should not take part in providing equity capital especially to new undertakings and an amendment of the

Act may be made to allow the IFC to do this. The Corporation has rightly began to underwrite the shares of new concerns, and it should be allowed, when necessary, to convert its underwriting loans into equity capital in suitable cases. It is necessary that the operations of such an institution as the IFC should be as much flexible as was possible, subject of course to the ultimate control of the government.

Of the three ways in which the IFC may give financial aid to industries, it has adopted only the first method. It has underwritten the shares only recently nor has it guaranteed the loans of any concern. Recently the Shroff Committee has made a number of recommendations to enlarge the scope of activities of the IFC. First, the IFC should endeavour to give debenture-loans. Secondly, it should explore the possibility of converting the whole or part of loan given by it into equity capital on mutually agreeable terms. Lastly, it should examine the scope for lending jointly with banks or guaranteeing advances granted by banks and insurance companies. All these recommendations have been adopted by the IFC, and it has made significant progress both in under-writing and in financing industrial projects jointly with other financial institutions.

Industrial Development Corporations : A few years ago two industrial Development Corporations have been set up, one on the initiative of the World Bank and the other by the Government of India.

The first institution, called the **Industrial Credit and Investment Corporation** (ICIC) has been sponsored by the World Bank. Rs. 3·5 crores have been subscribed by institutions and individuals in India, partly by public offering and partly through private placement. Of the balance, Rs. one crore have been taken up by certain British investors (some of the eastern exchange banks, the Commonwealth Development Finance Company, several insurance companies and industrial firms), and Rs. 50 lakhs by American investors (the Bank of America, the Rockefeller Brothers and others). The Government of India has agreed to grant an interest-free loan of Rs. 7·5 crores to this institution for 15 years, to be repayable after this period in 15 annual instalments. This sum represents the counterpart funds of steel supplied by the U.S. Government under the technical assistance programme. The Government of India has also agreed to guarantee the loan the World Bank has agreed to give to the Corporation. The World Bank

has agreed to give a loan of Rs. 5 crores to the Corporation. Thus the Corporation is assured from the beginning of a large supply of funds aggregating Rs. 17·5 crores, and its resources could be expanded upto Rs. 50 crores as it would have the power to borrow upto three times the amount of its initial resources.

The main function of the ICIC is to encourage industrial development in the private sector by helping the establishment of new industries or the expansion and rehabilitation of existing concerns. It may subscribe to the share capital or underwrite the issue of such concerns. It may prove to be an important agency for attracting foreign capital for investment in Indian industries. Through its connections abroad it will be in a position to help Indian industry to meet its needs for technical knowledge and managerial experience by getting experts from aboard. Where it takes up shares or underwrites the issue of shares, it will try not to have a controlling interest in the capital structure or the management of the industries concerned. Since its inception in 1955, the ICIC has granted loans totalling Rs. 31·41 crores to 95 companies. These loans have been granted in the form of loans and guarantees, partly in foreign currencies and partly in rupees. It has also undertaken under-writing operations and provided direct subscriptions to ordinary and preference shares. In these various ways it has taken some part in broadening the investment in this country.

A government-sponsored National Industrial Development Corporation (NIDC) has been set up. This institution is owned by the state with an initial capital of Rs. 1 crore. Other funds, as necessary, would be provded by the government. Its primary aim is to encourage the setting up of risky, large, capital-consuming projects which the private sector is unable to develop. A basic feature of the scheme is that industries started by this Corporation would be gradually transferred to the private sector when these become fully established.

While there is ample room for such institutions, care should be taken to see that these do not compete with the one another or with the IFC, which is also designed to provide long-term capital to private industry. It is, therefore, necessary to have clear ideas about their respective fields of operation. As the IFC has so far confined itself to providing loan capital, the best course for these Corporation would be to specialise in the provision of equity capital for industrial concerns.

They should work in co-operation with stock exchange firms so that the new issues might receive greater public response.

Medium-term credit : By the end of 1956, several institutions have been set up for meeting the long-term credit needs of industry. It was soon felt that the absence of an institution for the grant of medium-term loans to industry was an important defect of our money market organisation. It is common knowledge that though the loans granted by the banks are repayable within a short-time, a certain portion of these loans has to be renewed so that they are virtually medium-term loans. This was a makeshift arrangement with some undesirable locking up of banking funds. As monetary stringency became very acute in the busy seasons of 1956-57, it was considered that the locking up of banking resources in medium-term loans was one of the causes of such stringency. As their funds are invested in medium-term loans, banks are not able to devote their resources to meet the demand for short-term loans. To remedy this situation, the Government of India set up the Re-Finance Corporation for meeting the medium-term credit needs of industry.

The **Re-Finance Corporation** had a share capital of Rs. 12·5 crores, subscribed by the Reserve Bank of India (Rs. 5 crores), the State Bank of India, other banks and the Life Insurance Corporation. The Government of India placed with the Corporation the American counterpart funds of Rs. 26 crores as an interest-bearing loan for 30 years. Loans under this scheme were for 3 to 7 years, and the maximum amount of loan to any one borrower was not to exceed Rs. 50 lakhs. Each of the participating banks was given a quota, and within this quota it might offer certain types of loans to the Corporation for discount. Banks would have to assume the full credit risks on such loans submitted to the Corporation for discount.

The Industrial Development Bank of India (IDBI) :—The latest in the field of specialised institution for the supply of finance to industries is the Industrial Development Bank of India. It has been set up in 1964 with an authorised capital of Rs. 50 crores subscribed by the Reserve Bank of India. The authorised capital may later be increased to Rs. 100 crores. The Bank has started operations with an issued capital of Rs. 10 crores and is entirely owned and managed by the Reserve Bank of India, the Central Board of Directors of the latter constituting the Board of Directors of the IDBI.

The IDBI is authorised to receive loans from the central government from time to time, including one of Rs. 10 crores, interest free, repayable in 15 annual instalments. It may also borrow from the Reserve Bank including term borrowing from the National Industrial Credit (Long-Term Operations) Fund set up by the latter on July, 1964 with an initial credit of Rs. 10 crores. It may raise funds from the market through (*a*) the issue of bonds and debentures with or without government guarantee, and (*b*) the acceptance of deposits of not less than one year's maturity. The central government may also set up a Special Development Assistance Fund to enable the IDBI to provide financial assistance to projects which are not in a position to secure loans from banks or other agencies on account of certain special reasons such as low rates of return on investment etc.

The IDBI is to function both as the apex body for other lending institutions and as a primary lending institution for the industrial concerns. It may refinance the term loans of 3 to 25 years maturity made to industrial concerns by the various institutions such as the IFC, SPC and other as notified by the government. It should be noted here that the Refinance Corporation has been merged in the IDBI. It may also refinance the term loans of 3 to 10 years' maturity made to industrial concerns by the scheduled banks and the State Co-operative Banks. It may also subscribe to the stocks and bonds of the IFC, SFC's etc. It may also provide financial aid through the rediscounting of bills, promissory notes etc.

In addition to the provision of long-term re-finance to the various institutions participating in the grant of term loans to industrial concerns, the IDBI may also directly finance industrial concerns through the purchase or underwriting of shares and debentures, provision of guarantee for deferred payments due from such concerns as also for loans raised by the latter from the scheduled banks or state co-operative banks or from the open market. It may also guarantee the obligations of these lending bodies on account of their underwriting operations.

Since its inception in July, 1964, the IDBI has sanctioned total assistance amounting to Rs. 131·11 crores, out of which Rs. 57·77 crores have actually been disbursed. Out of this amount Rs. 106·38 crores were sanctioned during 1965-66, consisting of Rs. 25·15 crores for refinance, Rs. 41·79 crores as direct loans to industrial concerns,

Rs. 10·75 crores for underwriting of shares and debentures, Rs. 1·84 crores as subscription to shares and bonds of financial institutions, Rs. 16·75 crores by rediscounting of bills and Rs. 10·10 crores on account of guarantees of loans and deferred payments. Most of the direct assistance provided by the IDBI went to new industrial projects, and the Bank has decided to give preferential treatment to defence and export oriented industries, industries producing essential consumer goods etc. Since March, 1966 the Bank has introduced a Participation Scheme under which it assumed a measure of risk-sharing with the other financial institutions, agreeing to participate in loans granted by the latter to the maximum extent of 75 p.c. (80 p.c. in exceptional cases).

The ownership and management of the IDBI by the Reserve Bank have been questioned by a number of writers. It is not desirable to entrust the management of this important institution to the Central Board of Directors of the Reserve Bank which must already be fully occupied with the more important task of managing the monetary affairs of the country. Moreover, central banking activities are of a different nature from those of long-term industrial financing requiring different types of skill and expert knowledge.

Unit Trust of India: Another new comer in the realm of industrial finance is the Unit Trust of India which has been established on February 1, 1964 with an initial capital of Rs. 5 crores. This capital has been subscribed by the Reserve Bank, the LIC, the State Bank and its subsidiaries, the scheduled banks and other financial institutions. It is to be managed by a Board of Trustees, consisting of the Chairman appointed by the Reserve Bank., which also nominates 4 other trustees, one trustee each nominated by the LIC and the State Bank and 2 other trustees nominated by other financial institutions. The Trust may also borrow from the Reserve Bank and other banks and financial institutions. It is exempted from payment of income tax, super tax and other taxes on its income.

The Trust issues units of the face value of not less than Rs. 10 or not more than Rs. 100. These units will be sold at prices to be determined by the Trust from time to time on the basis of their estimated market value. The buyers are allowed to buy as many units as they like. These units may at any time be resold to the Trust at prices determining by the latter, thus providing a high degree of liquidity to the

unit-holders. These units are to be sold to numerous subscribers, particularly the small investors, and the proceeds of the sale of these units are to be invested by the Trust in government securities and in first class industrial securities. Not less than 90 p.c. of the net incomes obtained from these investments are to be distributed among the unit-holders in the form of dividends. The unit-holders were paid dividend at the rate of 6·1 p.c. during the 1st year of the operation of the Trust, and 7 p.c. during the 2nd year. The income from the units is free of income tax to the extent of Rs. 1000.

The Unit Trust is meant for the benefit of the small investors who do not possess enough funds or the knowledge to participate in the industrial concerns. They purchase the units and are thus able to enjoy the benelts of reasonable rates of dividend with the minimum of risk. The Trust has not only invested its funds in the purchase of securities of old and well established industrial concerns but has also provided underwriting facilities for new issues.

The problem of foreign capital : One aspect of the small amount of savings in this country is that in the early days most of the industrial concerns were established by foreigners with foreign capital. As industrialisation proceeded, Indians came forth with some capital for investment in industries. But even at the present day foreign capital pays a significant role in financing industries in this country. A survey conducted by the Reserve Bank showed that on June 1959, the total foreign investment in India amounted to Rs. 610·7 crores, of which the major portion (*i.e.*, Rs. 400 crores or 66 p.c.) was supplied by Great Britain. The U.S.A. invested only Rs. 82 crores and Canada Rs. 9 crores. Among particular industries foreign capital is important in the jute industry, tea, coffee and plantation industries, mining industries, match industry, oil industry, soap industry, tramways and electricity undertakings etc. In recent years while a number of foreign concerns have sold their business to Indians, a considerable section of foreign companies has adopted the practice of converting their business into Indian companies with rupee capital, selling only a small portion of their share capital among Indians. According to a study made by the Reserve Bank of India, the total foreign investments made in the private sector (other than banking) amounted to Rs. 690·5 crores in 1960 of which UK's share was Rs. 446·4 crores (65 p.c.) and American investments amounted to Rs. 113 crores (16 p.c.). In banking, the total foreign

liabilities amounted to Rs. 73 crores. Our foreign liabilities in the official sector were Rs. 1205 crores in 1960.

Before the advent of Indian independence, Indian opinion was definitely hostile to the entry of foreign capital. The most important reason for such a feeling was mainly political. The foreign businessmen, mostly Britishers, opposed the political advancement of this country. Moreover, it was feared that foreigners, if allowed to come in freely, would secure a stranglehold over the economic life of the country to the detriment of the real interests of the people. There were also a few cases where as in shipping foreign capital with its large resources established a monopoly and opposed the entry of Indian concerns often by adopting unfair business practices like rate-cutting etc.

There were also other ways in which industrial development by foreign capital did not always promote the interests of this country. Foreign businessmen usually employed their own nationals in positions of responsibility. Indians were employed only in the lower ranks, as clerks or peons. There was also some unwillingness to train up Indian apprentices in positions of trust and responsibility. Lastly, development by foreign capital meant that the profits, which were often large, were sent out of India and enriched other countries. Moreover, foreign concerns naturally gave the first preference to considerations of profit to the neglect of the real interests of the country. The important but limited supplies of minerals were exported to other countries in the raw state, no attempt being made to manufacture them locally. Metaullurgical coal was exported in large quantities as it fetched good profit. It ought to have been conserved in the real interests of the country. ..

If foreign capital is brought in the form of share capital control over the industrial concerns would then remain with foreign firms, a step which might not always be desirable. If it comes in the form of loans it becomes a very rigid and costly method. The borrowing country has then to set apart large sums every year, to pay interest and to find large sums of foreign exchange when repayment falls due.

But when everything is said against foreign capital, one must also mention its good points. There is scarcely any under-developed country which has been able to develop its resources in the initial stages without the aid of foreign capital. The United States started on its industrial

career with the help of British capital. The political objection is no longer serious as our National Government is now quite competent to adopt suitable steps for the protection of the real interests of the country. It is also putting pressure on foreign concerns to appoint and train up more and more Indians in the higher posts, and the pressure is already bearing fruit to some extent. If foreign capital is allowed to develop any industry, profits would no doubt be taken away from the country. But this is a price we must pay for securing industrial development at a faster rate than would be possible solely with our own meagre resources. Moreover, foreigners bring with their capital technical know-how, without which it would not be possible to develop our industries. They have taught us the art of business management and helped in creating an industrial atmosphere which has been an important factor in luring Indian capital into industrial development. One must not forget the fact that foreign capital has borne the initial risks of industrial development. A number of them lost their capital before others succeeded and we have been able to benefit from their losses and mistakes. It has constructed the railways and other means of communication, without which industrialisation would have been postponed further.

Political independence and the need of securing a more rapid development of the economic resources have induced a welcome change in the public opinion towards the entry of foreign capital into this country. The Planning Commission has estimated that unless foreign capital comes into the country in considerable amounts the government would have to take resort to deficit-financing on an increasing scale to achieve the targets of planned expenditure. Some amount of foreign capital is of course coming in, especially from the World Bank, the government of the U.S.A. and governments of some countries sponsoring the Colombo Conference. Private foreign capital is also coming in to start particular industries (such as the oil refineries of the Standard Oil Company or the Burma Shell) or to work in partnership with Indian capital (as in the automobile industry, the chemicals industry etc).

Government policy. The government has announced a liberal policy for promoting an increased flow of foreign capital into this country. The Industrial Policy Statement of the Government of April 1948 and the Prime Minister's statement have sought to give assurances to foreign capitalists. Assurances have been given that (1) there would be no discrimination in the application of the general industrial policy between

Indian and foreign firms. (2) The government would provide reasonable facilities for transferring profits and capital to other countries, consistent with the foreign exchange position of this country. And (3) if the government decides upon nationalisation of industrial concerns, it would pay fair and equitable compensation to the foreign investors. In return, it was expected that the major share in the ownership and management of these concerns should be granted to Indians, and that they should train up Indians increasingly to hold high technical positions of responsibility. Even with regard to some of these conditions, the government has made exceptions in the case of a number of foreign concerns. For example, in order to encourage the establishments of oil refineries, the government has permitted them to retain the major share in ownership and management, and has granted exemption from certain provisions of the Indian Companies Act and the Industries (Development and Regulation) Act. A guarantee has also been given against nationalisation for the next 25 years.

These conditions are quite reasonable and ought to remove impediments from the free flow of foreign capital. At the present moment the only country from which foreign capital may come in large amounts is the U.S.A., though Russia and the U.K. have also helped in the establishment of steel plants in this country. It would be better if attempts are made to reach agreements with capital-exporting countries which would allay their doubts and fears and might make the flow of foreign capital smooth. Another way to encourage the flow is to arrive at certain mutual fiscal arrangements under which foreign firms could be free from double taxation.

A Note on the Corporate Sector. Industrial development has everywhere been accompanied by the growth in the number of joint-stock companies, which facilitated the task of raising large amounts of capital through the sale of shares, stocks or bonds. This has also been the case in India. The first Companies Act was passed in India in 1850, and the principle of limited liability was incorporated in that act in 1857, so that the organisation of joint-stock companies was as old as the development of modern industries in India. By the end of the 19th century, the number of joint-stock companies had risen to 1340 and their paid-up capital amounted to Rs. 34·7 crores. In 1947, when India achieved independence, the number had risen to 21,853 and their paid-up

capital had increased to Rs. 478·7 crores. As regards the industrial pattern of these companies, as was quite expected, the vast majority of these companies were set up to run the traditional industries. Thus by the end of the 19th century six traditional industries of the country, viz., cotton, jute, paper, coal, tea and coffee plantations, accounted for about 88 p.c. of the total paid-up capital of all joint-stock companies. The twentieth century had witnessed greater industrial diversification, as a result of which, the share of these traditional industries in the total paid-up capital of all companies was reduced to 32 p.c. The subsequent diversification of industrial development in the last 18 years had further brought down the share of these traditional industries to 22·5 p.c. of the total paid-up capital of all companies.

The growth in the number of resources of the joint-stock companies has been quite substantial during the subsequent 14 years. The number of such companies increased from 21,853 in 1947 to 29,874 in 1955-56 and then came down to 26,108 in 1960-61. This reduction in number after 1956 had been due to the policy pursued by the Company Law Administration for weeding out dormant and moribund companies from the register, and thus generally to strengthen the corporate sector. In spite of this decline in numbers, the total paid-up capital of all companies had increased from Rs. 478·7 crores in 1946-47 to Rs. 1724·6 crores in 1960-61, *i.e.*, by more than 250 p.c. in course of 14 years. This growth in the total paid-up capital of the corporate sector is certainly remarkable and reflects the nature of industrialisation that has been achieved during the 10 years of planning. In fact, the total paid-up capital of all companies had risen from 775·5 crores in 1950-51 to Rs. 1724·6 crores in 1960-61, i.e., by 122 p.c. in 10 years, or by an average of 12 p.c. per year.

The importance of the corporate sector in the structure of large-scale industries in India will be obvious from the fact that 92 p.c. of the total factory output in the 28 major industries of the country came from the factories owned by the companies. Moreover, the output produced by these companies amounted in 1957-58 to about 12 p.c. of the total national income of the country, and, during the ten years ending 1957-58 their output has been estimated to have increased by about 50 p.c.

One remarkable development has been the increase in the number of government-sponsored companies in each of which the government

holds 51 p.c. or more of the total share capital. By the end of the year 1955-56, the total number of such companies was 61 and their paid-up capital amounted to Rs. 66 crores. During the next five years, the number of government companies has more than doubled and the paid-up capital had increased nearly eight-fold. The share of the paid-up capital of the government companies in the total paid-up capital of all companies had risen from about 6 p.c. in 1955-56 to about 29 p.c. in 1960-61.

Another significant trend has been the increase in the role of large companies in the corporate sector. An overwhelming proportion of the companies consisted of small concerns whose paid-up capital was below Rs. 5 lakhs. These formed about 90 p.c. of the total, but held only 12 p.c. of the total paid-up capital of all companies. At the other end the big companies whose paid-up capital was Rs. 1 crore or more numbered only 156 in 1957-58, *i.e.*, less than 0·6 p.c. of the total, whereas their paid-up capital amounted to 46 p.c. of the total paid-up capital of all companies in that year. The number of these giant concerns increased after 1950-51, and 304 giant companies had been floated during the First and the Second Plan periods with a total authorised capital of Rs. 1278 crores. Of these the government companies numbered 43 with a total authorised capital of Rs. 689·0 crores. Thus the giant-sized concerns occupy a dominant position in the corporate sector of our economy and as their number has been increasing in recent years, the trend towards oligopolistic development had no doubt been much accelerated. Of the new companies floated during the two plan periods, excluding the government companies, these giant concerns in the private sector numbering only 26 (with a paid-up capital of Rs. 1 crore or more) had an authorised capital of Rs. 583·3 crores, which was more than 51 p.c. of the total authorised capital of all non-government companies floated during this period.

Questions

1. Discuss the merits and demerits of the managing agency system in India.

"Although in the initial stage the managing agency system played an important role in the development of industries in India, it has several drawbacks." Discuss.

2. What steps have been devised in recent years to improve industrial management in this country ? Comment on the recent legislation on the subject.

3. Examine the proposals of the Company Law Committee for reforming the managing agent system.

4. Describe the sources of supply of capital available for the development of industries in India. What measures would you suggested for improving the system ?

5. Give a critical account of the organisation and functions of the Industrial Finance Corporation.

6. Write notes on the organisation and functions of the Industrial Development Corporation.

7. Discuss the scope of foreign capital in the economic development of India to-day. What are the sources from which foreign capital may be obtained ?

8. Examine the present policy of the Government of India regarding the investment of foreign capital in this country.

9. Describe the measures that have been taken in the last ten years to improve the organisation for the supply of long-term finance to Indian industries. (C. U. B. Com. 1957).

CHAPTER 23 THE STATE AND INDUSTRIAL DEVELOPMENT

Government's industrial policy before 1947 : Throughout the whole of the 19th century the Government of India followed in general a policy of laissez faire, and except in the case of a few industries did practically nothing to foster the development of industries in this country. The only exceptions are the tea industry and the railway industry, where the government took some positive steps to encourage their development. A change took place in the 20th century with the establishment, in 1905, of a separate Department of Industries and Commerce by the Government of India. The two Provincial Governments of Madras and U.P. adopted a more positive policy of active participation in the development of industries and started a few factories and granted loans to others. This aroused the hostility of the European business interests, and at their instigation, the Secretary of State, Lord Morley, deprecated such activities on the part of the governments concerned. Then came the first world war when for the first time the government felt that the development of at least some industries was essential from the military point of view. The result was the appointment of an Industrial Commission by the Government of India. That Commission, in its report, urged the government to adopt a more positive policy towards industrial development. In the meantime the government had set up a Munitions Board for the purpose of buying army requirements as far as possible in India. This gave some stimulus to the growth of industries, especially those catering for war materials. Following the recommendations of the Industrial Commission, the different Provinces started separate Departments of Industries, and passed State Aid to Industries Acts under which the government granted long-term loans to small-scale industries for their growth and development. In 1922, the Government of India established the Indian Stores Department, and this Department was entrusted with the task of buying goods required by different departments of the government from Indian manufacturers. Meanwhile, a Fiscal Commission was appointed to examine the question of the proper tariff policy.

The first Fiscal Commission recommended the adoption of a policy of discriminating protection according to which industries were to be granted protection provided that they satisfied three conditions. This

was accepted by the government and between 1924 to 1939, a number of industries such as the iron and steel industry, the cotton textile industry, paper industry etc., were granted protection by the government. But the policy of protection was carried out only half-heartedly.

During the second world war the government was forced to take some interest in the development of industries. They announced certain modifications in the policy of protection and gave a guarantee that industries established to meet war requirements would be protected in a suitable manner after the war. A Board of Scientific and Industrial Research was set up for conducting research on industrial problems. The need for adopting an economic plan for the development of industries was accepted by the government.

The advent of independence in 1947 changed the whole position. The government is now increasingly conscious of the need for fostering industrial development. To carry out this objective, the government announced, in April, 1948, its industrial policy.

Government's industrial policy of 1948 : This industrial policy statement was issued by the government in April, 1948. The statement pointed out the extent to which the state would itself own and manage industries, and the extent to which it proposed to exercise general control and supervision over the private sector. It also sought to lay down the different ways in which the government proposed to extend aid to industries left to private esnterprise.

The ideal envisaged by the statement was a sort of mixed economy in which both state-managed units and private enterprise would each play their part in the industrial field. The statement divided industries into three groups, *viz.*, industries to be wholly owned and managed by the state (the pure public sector), industries in which both state-managed units and private firms would exist side by side (the public-cum-private sector), and lastly, industries to be left to purely private enterprise, subject to the control of the government (the private sector). The manufacture of arms and ammunitions, the production of atomic energy, railways would remain exclusively under the public sector. Actually the state already owned all units in these industries and private enterprise is unlikely to be interested in these lines. Secondly, such industries as coal, iron and steel, aircraft manufacture, ship-building, manufacture of telephone, telegraph and wireless apparatus (excluding

radio-receiving sets), and mineral oils would belong to the public-cum-private sector. Government proposed to set up new units in these lines. Existing concerns would be allowed to operate for a period of ten years at the end of which the position was to be reviewed. Lastly, a large number of other industries like salt, automobiles and tractors, generation and distribution of electricity, electrical engineering, heavy chemicals, fertilisers, non-ferrous metals, rubber manufactures etc., would be left to private enterprise, subject to the control and regulation by the state in certain matters. For example, the State proposed to regulate the licensing and location of factories, and to adopt certain measures for improving labour condition and for ensuring satisfactory labour-capital relations etc.

Attention was also to be paid to the development of cottage and small-scale industries and for this purpose, the government proposed to set up a Cottage Industries Board. The government would also examine the question how far and in what manner these industries could be co-ordinated and integrated with large-scale industries.

The industrial policy statement of 1956 : The statement on industrial policy issued in April, 1948 remained in force for 8 years. In the meantime the Parliament accepted the policy of introducing the socialistic pattern of society as the principal objective of this country. The government felt that this required a revision of the industrial policy, and in April, 1956, a new Industrial Policy statement was issued by the government.

This industrial policy divided industries into three categories. In the first category are industries the future development of which will be the exclusive responsibility of the State. These include 17 industries like the manufacture of arms and ammunitions, atomic energy, iron and steel, coal. mineral oils, aircraft, air transport, railways, ship-building, telephones, generation and distribution of electricity etc. All new units in these industries will be set up only by the State. But the existing private units may also be allowed to expand, and the State may also invite the co-operation of private enterprise in the establishment of new units.

In the second category, there are a number of industries (12 in all) like aluminium and other minerals, machine tools, fertilisers, synthetic rubber. road and sea transport. antibiotic and other essential

drugs etc. The State will increasingly establish new undertakings in these industries. At the same time, private enterprise will also be encouraged to set up new units.

All the remaining industries will fall in the third category. Their development will ordinarily be left to private enterprise, though the State may also set up new units. The State will also continue to foster these industries through the development of transport, power and other services, by providing financial aid, and adoption of appropriate fiscal and other measures.

This division of industries into 3 categories does not imply that they are being placed in water-tight compartments. The State may start a new unit in any industry even in the third category "when the needs of planning so require, or there are other important reasons for it." In appropriate cases, privately owned units may be permitted to produce an item falling within the first category "for meeting their own requirements or as by-products."

The statement also lays emphasis on the need and importance of developing cottage and small-scale industries, for the adequate training of personnel, and for the provision of amenities and incentives to workers. It also stressed the importance of securing a balanced development of the economy and of decentralisation of authority.

The most important difference between the 1948 Policy statement and the present one is with regard to the policy of nationalisation. The 1948 Resolution laid it down that private undertakings falling within the field reserved for the exclusive development by the state would be permitted to operate for 10 years, at the end of which (*i.e.* in 1958), the government would determine whether to nationalise them or not. The 1956 Policy statement has omitted all such possibilities. Instead, it has stated in effect that existing privately owned units in category A industries would be allowed to expand, and the state might help them to expand by the grant of financial assistance, if necessary. Thus one may say that the present policy marks an important departure from the policy of nationalisation of private industrial units operating in the predominantly public sector. On the other hand, it permits the existing privately owned units to develop along with state-owned undertakings in all the three categories of

industries. Thus private enterprise has been given a new opportunity to justify its existence in a socialistic state.

The Industries (Development and Regulation) Act of 1951: In the Industrial Policy statement of April, 1948, the government stated that in regard to certain groups of industries to be left to private enterprise for development the government would retain some control over their working. A bill embodying the government's proposals regarding the regulation and development of these industries was later introduced in the Parliament, and finally passed in 1951. In order to emphasize that the purpose of the Act is not control, it was called Industries (Development and Regulation) Act.

The Act provides, in the first instance, for the licensing of factories. All persons wanting to start a factory with a capital of more than one lakh of rupees would be required to take a licence from the government. All existing factories would have to take a licence within 6 months from the date of enforcement of the Act.

Businessmen carrying out substantial extensions to their factories would also have to apply for licence. Before granting a licence the government may impose certain conditions as to the location of the factory, the minimum standards as to the size of the factory etc.

Secondly, the Act authorises the government to set up Development Councils for any industry or groups of industries included in the schedule of the Act. This Council is to consist of persons representing the interests of businessmen, workers, and consumers and of persons possessing special knowledge (teachnical or other aspects), of the industry. It will be the duty of each Development Council "to increase the efficiency of the industry, to improve or develop the service that it renders or could render to the community." For this purpose, it is to suggest norms of efficiency for obtaining maximum production, improving quality, avoiding waste and reducing costs. It is also to recommend targets for production, to recommend measures for the fuller utilisation of installed capacity and to promote scientific and industrial research and improve technical training facilities. This is the positive side of this legislation and it is through Development Councils that the government expects to encourage the development of industries.

Thirdly, the Act authorises the government to take certain punitive measures against industrial concerns which are found guilty of certain

offences. If, at any time, the government finds that there is likely to be a substantial decline in production or deterioration in quality or an unjustified rise in prices, or that concern is being managed in a manner likely to cause serious injury or damage to the interests of the consumers, it may make an investigation and issue appropriate directions to the concern regulating its production or controlling prices etc. If the government finds that it is not carrying out these directions, it may take over the management of the concern. When, however, the purpose of the order is fulfilled, the government may cancel the order and return the concern to the owner.

Lastly, the government was also authorised to establish a 30-man Central Advisory Council, consisting of members representing the interests of owners, workers, consumers and others. The main function of the Council would be to advise the government on matters relating to the regulation and development of industries.

The provisions of the Act have been criticised by the business interests. It has been urged that it places large and undefined powers of regulation over industries in the hands of the government. Even with the best of intentions, the machinery of the government is extremely slow and halting, and the consequent delay involved in the grant of licences would often create difficulties in the way of new industrial units. Moreover, there are, and have been, no reasons why the government should require similar power for established industries like sugar, cement, tea, paper etc., as it wanted for new industries. The provisions authorising the government to take over the management of a concern in the event of certain happenings have also been criticised as being too drastic. The Act "is hardly calculated to produce the atmosphere in which venture capital, however venturesome. can come forward."

Much of this criticism is unfounded. The provisions regarding the taking over of a concern are meant to be applied to extreme cases, and ample safeguards (*e.g.*, consultation with the Central Advisory Council etc.) have been incorporated to prevent abuse. As regards the positive powers of determining the location, minimum size etc., these are essential if industrial development is not to proceed in a haphazard manner in the future. The planning of future development on sound and balanced lines cannot be secured without some system of licensing of new units and control over the location etc., of new undertakings.

The powers under the Act are essential if private enterprise is to act in conformity with the social and economic policy of the government. The provisions of this Act have been further amended in 1956 so as to include 31 additional industries within the scope of the Act.

State-owned enterprises : The State in India has owned and operated business concerns from early periods. The oldest of such concerns was the Posts and Telegraphs, a concern which is managed departmentally. The first industrial enterprise to be owned and managed by the state in India was the railways and certain factories for making munitions. The last war brought a great development in state enterprises. The government was forced to adopt state trading projects embracing almost the entire wholesale and most of the retail trade in foodgrains and other commodities in scarce supply. The end of the second world war witnessed the establishment of a number of important state enterprises. Several multi-purpose irrigation projects were started, of which the Damodar Valley Corporation was set up by an Act of the legislature as a semi-autonomous Corporation. In addition, the government established a number of industrial concerns like the Sindri Fertilizer Factory, the Chittaranjan Locomotive Factory, the Machine Tools Factory in Mysore, the Hindustan Ship-building Yard at Vishakhapatnam, and the Hindusthan Steel Ltd., at Rourkela in Orissa, the Hindusthan Aircraft Factory at Bangalore etc. The different State Governments have also adopted the policy of nationalisation of road transport. and special organisations have been set up to take over the road transport concerns. Some states have also started miscellaneous undertakings like the Haringhata Milk Supply Scheme etc. Lastly, the former States of Mysore, Hyderabad etc., also ran a number of State enterprises.

These enterpises have been organised in different forms. (*a*) Some like the Posts and Telegraphs etc., are managed departmentally by government officers responsible to the Ministers concerned. (*b*) Others like railways are organised under specialised Boards, consisting of a small number of men who are experts or officials in these concerns. (*c*) The autonomous public corporation form of organisation has also been adopted, for example, in the case of the DVC. (*d*) In some cases separate companies have been formed consisting of the government and important industrial concerns to run the concern. This is the case with the Machine Tools Factory and the Hindusthan Steel Ltd., etc.

State trading : Under the impact of modern conditions, governments in many countries had to assume a number of trading functions. This tendency became specially prominent during the last world war when special institutions were set up in different countries for the bulk purchase or sale of different commodities. The British government established the U.K. Commercial Corporation and the U.K. Raw Cotton Commission. The Government of India had also to undertake a number of trading functions for the bulk purchase of food-grains in foreign countries and their imports into India. Technically the term, State Trading, implies the import or export of commodities by the State or State-owned agencies on a monopolistic basis with a view to their re-sale.

During the last world war the Government of India had to exercise complete monopoly over the import of food-grains, fertilizers, steel, non-ferrous metals, raw cotton etc. Though this was done by government departments, there was constantly a talk of setting up a special agency to handle the import and export of a number of commodities. The question of setting up such an organisation was referred by the government to a Committee in 1949. and the Committee issued its report in 1950.

The Committee on state trading recommended the setting up of a State Trading Corporation which should be an autonomous body with an authorised capital of Rs. 10 crores and an initial capital of Rs. 2 crores. The Central Government should hold 51 p.c. of the shares, the rest to be subscribed by the State Governments and private investors. The Board of management was to consist of government representatives and of practical businessmen. It would undertake activities like the promotion of the export trade in the products of cottage industries, and should also handle the export and import of other commodities like food-grains, fertilizers, raw cotton etc.

There is no doubt that certain advantages would follow from the establishment of such a State Trading Corporation. It would, then, be possible to secure a more effective enforcement of grading and standardisation of commodities for export. It is well-known that one of the principal difficulties hampering our export trade is the lack of suitable grading and standardisation. It would be easier to introduce proper grading and standardisation if the export trade is handed over to the Corporation. Secondly, such a Corporation could adopt special

measures for the promotion of export trade in different markets. It can, for example, use national banking, shipping and insurance service, thereby encouraging the development of such services in the country. Thirdly, it would enable the government to fulfil its contracts formed with other countries under different bilateral trade agreements, specially in cases where private enterprise might fail to import or export on the required scale. Fourthly, such state trading is necessary from the point of view of the planning of our foreign trade. Any plan for the economic development of the country would involve regulation of imports. As our foreign exchange resources would be limited, we would have to exercise careful economy, with regard to the import of both essential and non-essential goods. Such a restriction of imports could of course be achieved by the present system of import control. But the method of import control in this country has given rise to many difficulties on account of frequent changes of policy, overcentralisation, inadequate appreciation of the needs of trade etc. A State Trading Corporation might avoid these defects. Lastly, state trading means centralised buying of imports or centralised marketing of exports. Such bulk purchase or sale would yield some saving through the elimination of middlemen's commissions. It would also enable this country to keep import prices at a reasonable level, or to practise discrimination in different export markets. India's collective buying capacity is a fairly important factor in the world market in the case of many commodities, and so it would enable her to procure imports at more favourable prices.

But such state trading may also be attended with grave risks. In the first place, state trading involves centralisation of trade in the hands of one organisation. This would result in the severance of connections between domestic and foreign traders—connections which have been developed over a long period of time. Tastes and habits vary from one area to another and different types and qualities are needed to satisfy the demand in different consuming areas. Individual importers are often accustomed to draw supplies from particular exporters or importers. Centralised buying would disrupt these normal channels of trade and the existing pattern of distribution. The disadvantage resulting therefrom would undoubtedly outweigh any possible benefits from state trading.

It has, for example, been complained that the state trading in raw cotton in the U.K. has resulted in mills being compelled to buy unsuitable

types and qualities of raw cotton. Under a system of decentralised, competitive imports, the importer is in closer touch with the market than a State Trading Corporation could be. Secondly, the private importers are often able to cover their purchases by hedging or by sales in view of the comparatively small amount of their individual transactions. But when a State Trading Corporation enters into a bulk purchase agreement, it may not be able to cover such a large transaction by hedging or by sales to domestic buyers. When losses are anticipated a private trader may be able to act quickly and cut losses, but a State Trading Corporation will not be able to do so easily. It has also been stated that bulk purchase of imports, instead of securing lower prices, has, on the other hand, resulted in pushing up prices in the selling centres or export markets. Moreover, in spite of the bulk purchase of food-grains during and after the war, the Government of India was not able to secure any material price advantage. If state trading is to yield the maximum price advantage, the Trading Corporation must be able successfully to anticipate world trends in prices. It may be exceedingly difficult for a single institution to perform this function effectively, and any mistake would have adverse effects throughout the whole economy. Unless it becomes necessary on account of exceptional conditions, the best agency for this purpose is not State Trading, but the co-operative wholesale marketing organisation.

The problem of nationalisation of industries : The Industrial Policy Statement of April, 1948 laid it down that with regard to the majority of the basic or key industries, the question of nationalising them was to be held in abeyance for the next 10 years after which the position was to be reviewed. In India already a number of industries are under public ownership, such as the defence industries, and the railways. The State has also started a few factories for the manufacture of locomotives, fertilizers, machine tools etc. The question, then, arises with regard to the nationalisation of the basic or key industries like the coal industry, the iron and steel industry etc. It is claimed that the State should acquire all existing units in these industries.

Those who argue in favour of nationalisation of the basic industries usually point to the grave economic inequalities and the many social problems arising under private ownership of the important means of production. State ownership of these industries would tend to minimise these problems and result in securing a greater equality of incomes. There are also special reasons for nationalising particular

industries. For example, it is well-known that the organisation of the coal industry in India is extremely inefficient. Most of the mines are of uneconomic size and so are not in a position to adopt cost-reducing measures like mechanisation etc. In view of the limited reserves of metallurgical coal, conservation of such coal is essential in the national interest. But such conservation could not be carried out properly so long as the industry remained in private hands. Thirdly, the question has assumed important in India on account of the fact that some of the basic industries are under foreign management. There is, for example, a demand for nationalising the jute industry on the ground that jute mills, being dominated by foreigners, have exploited jute-growers who are completely unorganised and so are helpless.

Those who oppose this policy generally point to the delays and inefficiencies of public administration. State management ultimately means management by public officials who are notoriously fond of red tapism, and who do not usually possess the same incentive in managing a concern efficiently as is possessed by private owners under the spur of profit motive. Moreover, there is a dearth of trained personnel in this country, and if attempts are made to nationalise different industries. it might cause serious dislocation. Thirdly, the government possesses only limited financial resources. Is it not better that such resources should be spent for starting new industries, thereby enriching the country than for the acquisition of existing units ? Lastly, the existing defects which are supposed to follow from private ownership can be remedied by an appropriate tax policy, which can be suitably manipulated so as to reduce inequality of incomes without impairing incentive. The dangers of nationalisation are far greater on account of the inefficiency, inexperience and corruption of public officials than any difficulties that may attend private ownership of the basic industries. Whatever the validity of arguments on both sides, there can be no doubt that the present is not a suitable time to carry out the policy. We should now devote more attention to branch out into new directions, opening out new fields than waste time and energy in acquiring units in industries which have already been developed.

Questions

1. Describe the policy pursued by the government towards the development of industries. Are you in favour of the State's taking a more direct share in the industrial development ?

2. Comment on the Industrial Policy Statement issued by the Government of India.

3. Critically discuss the main provisions of the Industries (Development and Regulation) Act of 1951.

4. Discuss the merits of State Trading. Do you support the establishment of a State Trading Corporation ?

What is the justification for State Trading in India ?

5. Discuss the desirability or otherwise of nationalising Indian industries at the present moment.

CHAPTER 24

FISCAL POLICY AND INDUSTRIAL DEVELOPMENT

If we study the history of industrial development in different countries, we shall find that the vast majority of them granted protection to their industries at least in the initial stages. This was the case in Great Britain, Germany, Japan etc. The U.S.A. is even now protecting her industries heavily against foreign competition, though she is one of the foremost industrialised countries in the world. What part has the policy of protection played in encouraging India's industrial development ?

It should be remembered that when from the middle of the 19th century, industries began to grow up in India one by one, the government was dominated by free trade ideas. So import duties were levied for purely revenue purposes, and no attempt was made to grant protection to Indian industries. There was, however, a persistent demand in India for the adoption of a policy of protection. The Government of India had ultimately to yield and appointed in 1922 a Fiscal Commission to examine this question. The majority of the Commission advocated a policy of discriminating protection, which was accepted by the government. A minority advocated the adoption of a stronger policy of protection.

Discriminating protection : The Fiscal Commission recognised that there was ample justification for the adoption of a policy of protection in India. They laid special emphasis on the need for the grant of protection for the development of (*a*) industries essential for purposes of defence and (*b*) young industries which showed promise of future development. They also pointed to the necessity for securing a diversification of industries to reduce our excessive dependence on agriculture and on one or two industries.

But the majority felt that while the adoption of a policy of protection was justified, the grant of indiscriminate protection would impose a great burden on the consumers and would harm the real interests of the country. So they recommended that protection should be *discriminatingly* granted. All industries applying for protection should not be protected. But a careful selection was to be made, and only those industries were to be given protection which showed possibilities of development in the near future. Each application for

protection was to be thoroughly examined by a Tariff Board, composed of experts on the subject. The Commission laid down three conditions which should be satisfied by the applicant industries before the Tariff Board could recommend them for protection.

(*a*) The industry must be one possessing natural advantages, such as the abundant supply of raw materials, cheap labour or large home market.

(*b*) It must be one which, without the help of protection, is not likely to develop as rapidly as is desirable in the interest of the country.

(*c*) It must be one which will be eventually able to face world competition without protection.

Apart from these, there were two other groups of industries which deserved special consideration by the government, *viz.*, industries essential for national defence, and key industries, (*i.e.*, industries whose products were used as raw materials by other industries). Moreover, industries which obeyed the law of increasing returns, and those which would be able to meet the needs of the whole market would deserve special consideration.

This was the famous "triple formula", which came in for a good deal of criticism at the hands of subsequent writers. It was claimed by the Fiscal Commission that this would enable India to develop her industries while avoiding the dangers attending a policy of protection. If properly carried out, it would protect only those industries which possessed comparative advantages and would soon develop into adults.

As a result, the burden on the consumers would be smaller, and there would be no danger of encouraging inefficient industries.

Achievements of the policy : Between 1923 to 1939, different Tariff Boards carried out in all 51 enquiries for protection or renewal of protection. The number of industries which actually received protection as a result of these enquiries was eleven, *viz.*, iron and steel including subsidiary steel industries, cotton textile industry, paper and paper pulp, matches, salt, heavy chemicals, sericulture, magnesium chloride, plywood and tea-chests, gold thread and sugar industry. The Tariff Board's recommendations for the grant of protection were rejected by the government in six cases. The Board rejected ten applications for protection. Of the protected industries, protection to the heavy chemical industry was granted only for a year and a half, and

that to the plywood industry was so altered that it received very little actual assistance. After the war protection was withdrawn from all industries with the exception of the Match and Sericulture industries.

There is no doubt that the Iron and Steel Industry justified the protection granted to it. In the paper industry, the production of printing and writing paper has developed to such an extent that no further protection may be required for this section when imports are freed from control. In the case of the sugar industry, development was almost phenomenal after the grant of protection, especially in respect to installed capacity and production. But regarding the lowering of costs the gains achieved have been almost negligible during these years. The case of the Match Industry is interesting on one account. It has no doubt expanded considerably after the grant of protection. But when the industry applied for the grant of protection, it was divided into two sections—an Indian sector producing two-thirds of the total production and a foreign sector controlled by the Swedish Match Trust. The application for protection came from the Indian sector which wanted protection against both imports and the foreign concern. In 1948, the Swedish Match Trust, known as the Western India Match Company, produced nearly 90 p.c. of the total output, while about 200 other Indian units produced the rest.

A review of the policy of discriminating protection during these years would show that in spite of all its defects, the policy enabled this country to secure three important benefits. In the first place, there was no doubt that the protected industries were enabled to increase their production by substantial amounts. Thus the output of steel ingots increased from 131,000 tons in 1922 to 1,042,000 tons in 1939, that of matches from 16 m. gross to 26 m. gross, of paper and paper board from 24,000 tons to 67,000 tons and of sugar from 24,000 tons to about 1 m. tons during the same period. The expansion of many of these industries yielded considerable benefits to cultivators. For example, the acreage under sugarcane increased from 26 lakhs in 1930-31 when protection was first granted to the sugar industry to nearby 36 lakh acres. Secondly, the grant of protection enabled these industries to remain comparatively unaffected during the world trade depression, when all other industries suffered considerably. Many of these protected industries were able not only to maintain, but actually to increase their volume of production during the major part of the depression. A third

way in which this policy conferred benefits was through the development of other industries. A number of other small industries (starch, chemicals etc.) have developed in the country, due no doubt to the availability of steel and steel products manufactured in India and to the existence of industries like paper, cotton textiles etc., which provide a market for their products. As regards the burden on the consumers, the Fiscal Commission of 1949-50 has, after an examination of the different aspects, came to the conclusion that "on balance the direct and indirect advantages to the community of protection of these major industries offset the burden on the consumers."

Criticism of the policy of discriminating protection. This policy came in for serious criticisms. In the first place, there were certain procedural defects. The government made the first mistake by not appointing a permanent Tariff Board. They appointed *ad hoc* Boards which could not take a long view of the growth of industries, or accumulate experience and build up an efficient body of technique and procedure. Moreover, the procedure that was followed involved a good deal of delay and uncertainty. The government took a long time to consider an application and to refer it to a Tariff Board. When it submitted its recommendations often after protracted enquiry, the government again took a long time to arrive at a decision. Such delays caused difficulties and uncertainty to the industries.

The triple formula on which the policy of protection was based was found to be extremely unsatisfactory. As regards the first condition that the industry should possess comparative advantages such as an abundant supply of raw materials etc., this was interpreted rather rigidly, resulting in a refusal of protection to many deserving industries. For example, the government refused to accept the Tariff Board's recommendations for granting protection to the glass industry or the worsted section of the woollen industry on the ground that essential raw materials were not available in the country. There are many cases of flourishing industries which import their raw materials from foreign countries. The locomotive manufacturing industry was denied protection in 1924 on the ground that the home market by itself was not large enough. But insistence on this condition ignores the possibilities of an export market, which, together with the home market, may open up prospects of economic production. Moreover, if the first condition is satisfied, the third becomes superfluous. The second condition was a

"truism" as no industry was likely to apply for protection if it was in a position to develop against foreign competition without the help of protection.

Thirdly, the insistence by the Commission that only industries already established should be given protection gave rise to a serious defect. An industry may possess large possibilities of development. But the promoters may hesitate to give a start without some promise of the grant of protection against foreign competition. Given that promise and fulfilment, the development of the industry may proceed at a rapid rate. But the government could not hold out such a promise according to the conditions laid down by the Commission.

The most fundamental defect of the policy recommended by the Fiscal Commission lay in the fact that they viewed protection as an instrument for enabling particular industries to withstand foreign competition. They failed to visualise protection as an instrument for securing general economic development. This has resulted in a lop-sided development of industries. The development of a particular industry is often dependent on the growth of other industries. Protection of particular industries without a positive effort being made to develop allied industries at the same time might have increased the total burden on the community. The problem of industrial development should be viewed as a whole, and the policy of protection should be treated as forming a part of an economic plan designed to secure the simultaneous and co-ordinated development of all the resources of the country.

The present fiscal policy : In the Industrial Policy Statement of April 1948, the government expressed its intention of reconsidering the tariff policy so as to make it an effective instrument for preventing unfair foreign competition and for promoting the utilisation of the country's resources without imposing unjustifiable burdens on the consumers. In pursuance of this policy, the government appointed a Fiscal Commission in 1948 to examine and report on the future fiscal policy. The Commission submitted its report in 1950 and made a number of recommendations on the proper fiscal policy designed as to fit into an overall plan of economic development.

The policy of protection is now to be looked upon, not as an instrument for protecting particular industries against foreign competition, but as an important means for promoting the economic develop-

ment of the country. This policy must be related to an overall plan of development of resources.

The Fiscal Commission then laid down certain fundamental principles on which the new scheme of protection was to be based. First, the different industries are to be grouped into three classes, *viz.*, (*i*) defence and other strategic industries, (*ii*) basic and key industries and (*iii*) other industries.

In regard to the first group of industries, they should be established and maintained with whatever degree of protection or assistance that might be necessary. Defence is greater than opulence.

In regard to the basic and key industries, the question of protection was to be left to the discretion of the Tariff Commission which would also determine the form and quantum of protection or assistance to be given to them. If development of any of these industries is included in the national Plan, this should provide enough justification for the grant of protection.

All other industries have been divided into three sub-groups, *viz.*, (*a*) industries for the development of which the Plan gives high priority, (*b*) industries which are complementary or ancillary to the basic and key industries in the planned sectors, and (*c*) other industries.

When an industry falling in this category applies for the grant of protection, the Tariff Commission was to apply two main conditions, *viz.*,

"Having regard to the economic advantages enjoyed by the industry or available to it and its actual or probable cost of production, it is likely within a reasonable time to develop sufficiently to be able to carry on successfully without protection or assistance ;

and/or

it is an industry to which it is desirable in the national interest to grant protection or assistance and having regard to the direct and indirect advantages, the probable cost of such protecion or assistance to the community is not excessive."

These conditions may be relaxed if the development of any industry is included in the Plan. In addition to these conditions, the Fiscal Commission gave its opinion on certain specific issues for the grant of protection. First, the fact that any particular raw material or raw materials needed for an industry are not available within the

country should not be used as an argument against the grant of protection, provided that the industry possesses other economic advantages. Secondly, in determining the comparative advantages possessed by an industry, not only its home market, but any possible export market should also be taken into consideration. Thirdly, ability to satisfy the needs of the entire home market should not be regarded as a condition for the grant of protection. It should be enough if the industry was in a position to meet the demand of a sizeable section of the home market within a reasonable time. Fourthly, in so far as other industries use the products of the protected industry as raw materials, they should be granted "compensatory protection", depending on the nature of the raw materials produced, the proportion that the cost of raw materials bears to the total cost of production of the industry, the nature of the additional burden likely to be imposed and other connected considerations. Firthly, as regards new or embryonic industries, the Tariff Commission should examine the facts and estimates relating to the industry and the nature of foreign competition it is likely to encounter, and then advise the government as to the assurance of protection to be given to the promoters of new industries. The need for such an assurance may be particularly strong in the case of industries requiring heavy capital outlay or involving a high degree of specialisation and plant equipment. Lastly, protection may also be granted to agricultural commodities subject to the following considerations, *e.g.*, the number of such commodities should be small and should be selected on the basis of their relative importance and the volume of employment they offer. The grant of any protection should be accompanied by the adoption of a programme of agricultural improvement, and it should be limited to short periods, never for more than five years at a time.

These principles, combined with the proposal to appoint a permanent Tariff Commission, are no doubt comprehensive and will remove many of the defects of the policy of discriminating protection. They lay emphasis on the fact that the question of the grant of protection should be subordinated to the needs of the economic plan for the all-round development of the resources of the country. Of course, it must be admitted that the first of the two conditions laid down for the grant of protection to industries falling in the third group contains the essence of the "triple formula", and if it is as rigidly interpreted as in the case of the policy of discriminating protection, it would have led to almost the same results. But the specific issues discussed by the

Commission and the insertion of the second condition rob it of much of its rigidity. And there will be no danger if the policy of protection is carried into effect against the background of the economic plan.

Methods of protection : Protection to an industry may be granted by levying import duties, by the grant of subsidies, by the application of quantitative restrictions, and by certain administrative measures.

The levy of import duties is the most usual method that is generally followed. Its chief defect is that it raises prices and imposes a burden on the consumers. Subsidies are financial grants given by the government to the manufacturers in the protected industry in order to enable them to sell at competitive prices. Its primary advantage is that it does not raise prices and does not impose any direct burden on the consumers. But instead of the consumers, it is the tax-payers who bear the burden of protection in this case. But there are important administrative disadvantages as the payment of subsidies requires careful control over the volume and quality of production. Under the method of quantitative restrictions, the government restricts the amount of imports of the foreign product to what it considers safe or reasonable quantities. Like the method of import duties, it also raises prices and may lead to the exploitation of domestic consumers by monopoly organisations, whether of foreign or domestic origin. Administrative measures include the manipulation of railway and shipping rates against imports, restrictions and prohibitions on imports on various pretext under the Sea Customs Act etc.

The Fiscal Commission accepted the fact that the main reliance was to be placed on the method of import duties. The method of quantitative restrictions should, in their opinion, be used only sparingly say, for temporary periods against abnormal imports. Subsidies are of course desirable, and for this purpose they recommended the creation of a Development Fund by the government which should set aside every year a portion of the revenues collected from protective tariffs. Subsidies could be granted from this Fund and the Commission expected that the creation of this Fund would remove some of the difficulties attending the method of subsidies and enable a consistent and continuing policy to be pursued from year to year. For example, the aluminium producers were granted subsidy for some time.

Obligations of protected industries : The grant of protection imposes considerable burden on the consumers. In return the protected

industries have also some special obligations to the community. The Fiscal Commission rightly points attention to the obligations.

First, the price policy of these units must be reasonable. If, however, the price rises and continues to stay above the reasonable level determined by the height of the protective duty, the government should take steps to regulate them.

Another obligation is with regard to the maintenance of the quality of the products in accordance with suitable standard specifications. Thirdly, an industry receiving protection should strive at adopting up-to-date methods and practices in production and distribution. Fourthly, it should be the duty of the protected industry to organise research for imported technique in suitable cases. It should adopt schemes for training apprentices and should provide opportunities for practical training to technical students and scholars. It should try to utilise indigenous raw materials to the utmost extent possible.

The list is not exhaustive, and the Commission recommended that it should be the function of the Tariff Commission to review the operation of protected industries from time to time to see whether they were carrying out their obligations. It was also to recommend suitable measures to the government for securing enforcement of the obligations in cases where they were being neglected.

Tariff Commission : The Fiscal Commission suggested the appointment of a Tariff Commission, which was to be a permanent body, consisting of five members including the Chairman. The Commission may co-opt assessors or advisers for particular purposes. The necessity for such a quasi-judicial authority in any scheme of tariff protection is now so universally recognised that the case for it needs no elaboration.

The Tariff Commission is to be entrusted with the following functions. First, it shall conduct enquiries when an industry applies for protection, or enquiries connected with allegations of dumping or enquiries for variations of protective duties or for tariff concessions under Trade Agreements. Secondly, it shall conduct enquiries into the effects of tariffs on the level of prices and cost of living or on other significant facts in the country's economy. Thirdly, it shall carry on investigations into the manner of working of tariffs, or into the price policy of the protected industries, or into any anomalies that may result from the working of protected duties etc. Lastly, apart from these *ad hoc* investigations, the Tariff Commission shall also carry out a

periodical review, preferably at the end of every 3 years, on the working of protective duties. These reviews should deal with the manner in which the obligations imposed on protected industries have been discharged, and the defects and deficiencies from which the protected industries are suffering, and any additional measures of assistance that these industries may require.

The reports of the Tariff Commission should contain an adequate analysis on which all their conclusions are based. They should present a clear picture of the over-all cost to the community of the protective duties and of any economic and social benefits that may be expected from the policy of protection.

Results of protectionism : The policy of protection was first adopted in 1923. Since then, cases of 108 industries that applied for the grant of protection have been examined by the various Tariff bodies. Of these, 66 industries were granted protection, and by 1960, 44 industries which received protection have been de-protected. That is, these had developed satisfactorily and stood in no need of protection. These industries had succeeded in stabilising themselves and expanded sufficiently to meet the demands of the home market as also to be in a position to export. In a number of case the withdrawal of protection was done because it was found that the prevailing levels of revenue duties were adequate to offset any cost disadvantages which were still present in some cases. In a few cases, the grant of protection was withdrawn after a short period as it was felt that the industry concerned was not making satisfactory progress, or that there was no possibility of the concerns stabilising themselves on an even basis. This, for example, happened in the case of phosphates and zip fasteners. The only instance where protection has been granted on an indefinite basis is the match industry were a high tariff is being contained to match a high excise duty imposed for revenue considerations. These are some of the industries that still enjoy the shelter of protective duties (in 1961)—*viz.*, aluminium, automobiles, bicycles, ball bearings, caustic soda, cotton textile machineries, dye stuffs, electric motors, matches, sericulture, sheet glass, soda ash etc.

Questions

1. Examine critically the nature and working of the policy of discriminating protection.

2. What is the new concept of protection adopted by the Indian Fiscal Commission of 1949-50? Explain in this connection the criteria which should be applied in considering applications of industries for protection.

3. "The Indian Fiscal Commission of 1949-50 approached their task from a new angle of vision and laid down new principles of protection." Elucidate this statement.

4. Discuss the functions of the Tariff Commission.

5. Discuss the principles of the protectionist policy adopted in India after 1949-50. (C. U. 1961)

CHAPTER 25

SOME INDUSTRIAL PROBLEMS

Location of industries : In the study of the location of industries, we examine the areas in which different industrial units have been established in the country, and then try to find out how far these are properly distributed from certain points of view. In theory businessmen are supposed to set up their factories in those places where their cost of production including the cost of transport is the minimum. But in practice they are not always guided by purely rational or economic considerations. Moreover, what may appear to be the best location from the point of view of businessmen may not actually be the most suitable in the national interests.

During the last hundred years a large number of industrial units have been established all over the country. Businessmen have followed their own considerations or instinct in selecting the places where to locate their factories. The result has been the heavy concentration of industries in the two States of Bombay and Bengal. In 1939, as much as 59·2 p.c. of the total number of factory workers were to be found in these two States. Since then there has been some tendency to set up industries in other areas. But even then in 1951, Bombay and West Bengal contained 54·3 p.c. of the total factory workers in India. If we include 3 other States, *viz.*, U.P., Madras and Bihar, these five States contained in 1951 88·4 p.c. of the total number of factory workers in India. The result has been that industrial development has been extremely uneven and lop-sided.

Not only are the industrial units concentrated mostly in two States, they have also tended to cluster round the two great cities of Calcutta and Bombay. The population of these cities has, as a result, increased by about 100 p.c. during the last 20 years. This is due partly to the concentration of industries, and partly to the influx of population from the rural areas. The large refugee population has also tended to move towards these cities as on account of the concentration of industries they provide the largest volume of employment in the country.

Such lop-sided development of industries has some adverse economic consequences. The concentration of industries in five States to the neglect of other regions has led to widely different money

incomes and standards of living in the country. These are highest in the two most industrialised States, while they are lowest in the comparatively backward States like Orissa, Assam etc. It is desirable that the benefits of industrialisation should be widely distributed all over the country, and should not be monopolised by a few States. Secondly, the congregation of industries in a few cities has given rise to serious evils. It has led to bad housing conditions, heavy congestion in transport and other public utility services and the consequent deterioration in public health. Thirdly, such congregation is also bad from another point of view. Bombing of these cities would disorganise the economic organisation of the country.

Hence it is necessary to take steps to change the location of industries. There is no reason why more sugar factories should be allowed to be established in U.P. and Bihar, which already possess a large number of such factories, and which are not ideally suited for the cultivation of sugar, and not in Madras or Bombay, where the climate conditions are more suitable for cane cultivation. Such dispersal of industries, where possible, is also desirable for the sake of strategic reasons. If industries are dispersed over the whole country, and not concentrated in big cities, the danger of aerial bombing would be lessened to that extent. Lastly, control over the location of industries is essential for a wider dispersal of the benefits of industrialisation over different parts of the country.

A tendency towards a wider dispersal of industries has become evident during the last 3 decades. Between 1921 to 1939, the share of Bengal in the total number of factory workers declined from 35 p.c. to 29 p.c.; that of Bombay from 25 p.c. to 23 p.c. while the share of Madras increased from 8 p.c. to 10 p.c. and that of the U.P. from 6 to 8 p.c. The cotton textile industry has also exhibited the same trend. Of the new mills, a larger numbers were being established in other States, away from Bombay. The same tendency is also to be found in the case of other industries like the sugar industry, the paper industry etc. In other words, many of these industries are tending to move towards the consuming centres.

State control over location : This tendency has got to be encouraged and speeded up. The State in India has, therefore, been obliged to take steps to influence the location of future industrial units. The Industries (Development and Regulation) Act of 1951 authorises

the Government of India to control the location of new factories. Under the Act, promoters of new factories would be required to take a licence from the government, and at the time of the grant of the licence, the government may lay down conditions regarding the location of the plant. By refusing to grant licences for new units, the government may thus prevent new factories being established in regions which it considers to be more or less saturated.

This power is, however, negative. Under this Act, the government may prevent new sugar mills from being established in Bihar. But it has no power to direct that such a factory is to be set up in Madras. This power may be used to prevent further concentration of industries in particular States or cities. But it will not enable the government to secure a better distribution of industrial units.

There are critics who are sceptical of the merits of State control over the location of industries. If a businessman selects a wrong site for the location of his factory, he will have to bear the loss. If he has to locate his factory on the orders of the government and cannot work it profitably, he can naturally claim that the government should bear the loss, or at least a part of it. Selection of business sites by government officials who are not well-versed in business matters is more likely to lead to wrong selections than when this is done by businessmen themselves.

Moreover, there are limits to the possibility of shifting industries to the under-developed areas. For example, industries which are raw material-oriented like the Iron and Steel industry can only be established near the sources of raw materials.

Rationalisation of industries : In recent times there has been a good deal of talk on the need or dangers of rationalisation of industries. The question has got to be studied dispassionately, keeping in view the standpoints of both the employers and workers.

The dictionary meaning of rationalisation is the application of reason to industry and the elimination of waste in labour, time and materials. As such it has always been present throughout industrial history. Industrial development has always proceeded through the adoption of methods designed to eliminate waste, and increase output and efficiency. But the word, "rationalisation" became specially prominent during the twenties of this century, in Germany and the U.K., when

it became associated with the attempt to eliminate surplus capacity in an industry through the closing down of uneconomic units and concentration of production in the more efficient units. As such it resulted in a series of amalgamations and capital reconstructions in different industries, and some substitution of labour by modernised plant.

In India, the need to introduce methods of rationalisation in different industries was increasingly felt in the thirties. At that time the majority of industries were faced with declining demand on account of the Depression and a search was being made to secure a reduction in costs to compensate for the fall in prices. In 1932, Tariff Board on the Cotton Textile Industry came to the conclusion that Indian mills were using more labour per unit of capital than was the rule in Japan or the U.K., as a result of which the cost of production was higher in Bombay than in the latter countries. Following the recommendations of the Tariff Board the Bombay Mill-owners' Association attempted to introduce schemes of rationalisation most of which, however, failed. The outbreak of the war stopped all this, a situation which lasted so long as there was a seller's market. But the emergence of a buyers' market in recent times with its declining demand has again given rise to talks about the need for introducing rationalisation in different industries, such as the cotton textile industry, jute industry, coal industry, sugar industry etc.

The report of the Cotton Textile Committee of 1953-54 has drawn attention to the need for rationalising methods of production in the cotton mill industry through the adoption of automatic looms over a number of years. The Jute Enquiry Commission of 1954 has also laid increasing stress on the introduction of rationalisation in that industry through the replacement of its worn-out machinery by modern equipment. The report of the Working Party on the coal industry (1950) has also advocated rationalisation through the amalgamation of smaller collieries to form bigger units and through increased mechanisation.

In general it would be fair to say that to-day in India the mangement favours rationalisation, while labour opposes it. Rationalisation is looked upon as a method for eliminating waste in production and for increasing output and improving efficiency. For this reason it is generally favoured by the producers. The opposition of labour is due to the fear, or almost certainty, that rationalisation would lead to considerable unemployment. Any change in organisation or method which

eliminates waste of time or labour tends to have the immediate effect of throwing some workers out of employment. The general feeling among the labour leaders is that in India where capital is scarce, and labour is plentiful, there should be no resort to methods of production which seek to utilise more capital and less labour. Moreover, even if it is admitted that rationalisation would lead to increased efficiency, lower prices, higher standard of living and so to more employment, these are, more or less, long-period effects. But in the long run we are all dead, and the argument provides no consolation to workers facing immediate unemployment. So in this conflict between the short-run and long-run effects of rationalisation, labour very naturally takes short-run dangers into account, unless the state or some other authority steps in and provides compensation to the unemployed, or makes alternative arrangements for their employment.

So a compromise is necessary in the interests of all parties. Labour must realise the inevitable fact that unless methods of rationalisation are adopted in different industries, costs of production cannot be reduced to the competitive level. The long-term maintenance of a high level of employment in each industry, the development of new avenues of employment and the improvement in the general standard of living,—all depend on the attainment of the highest level of efficiency by the Indian industry. Such levels of efficiency cannot be achieved except through the introduction of methods of rationalisation. But the management must also recognise the justice of the fear of labour. It may, therefore, be necessary for the state to control the pace of rationalisation in different industries in such a way as to minimise the burden of unemployment. Since some unemployment may become inevitable in a number of cases, the government should formulate, in co-operation with employers and workers, suitable schemes for the rehabilitation of unemployed workers through the grant of unemployment doles and through the organisation of facilities for retaining these workers for other jobs.

Combination movement in industries : In the western countries industrial development has been followed by the growth of monopolistic organisations. The same tendency has also been present in India. On account of the prevalent of the Managing Agency System, the combination movement has taken mainly the form of concentration of ownership and control in the hands of a few firms. Of the large number

of industrial firms in India, more than 600 of the largest industrial establishments are controlled by a small number of Managing Agency firms. Of these, more than 250 industrial establishments are under the control and management of nine leading British firms, *viz.*, Andrew Yule, Macleod, Martin and Burn etc. In the cotton mill industry, more than one-third of the productive capacity is in the hands of less than 30 Managing Agents. In Ahmedabad, 18 leading families control over four-fifths of the productive capacity in the cotton textile industry. Of the 85 jute mills working in India, 33 are controlled by 4 managing agency firms, and about one-fourth of the installed capacity in this industry is controlled by 2 British firms, Andrew Yule and the Macleods. In the coal industry, 4 firms of managing agents control about 30 companies. In the tea industry, Duncan Bros, a British managing agency firm, controls 25 tea companies, and in all 128 companies are under the management of 11 firms.

Apart from this concentration of management and control in the hands of a few firms, another characteristic has been the concentration of industrial power in the hands of comparatively small number of persons. As Dr. M. M. Mehta pointed out, nine leading families of India held nearly 600 directorships or partnerships in Indian industries.

Instances of combinations formed by the fusion of many firms are also to be found in India. The most prominent monopolistic organisation is the Swedish Match Trust, which, through its Indian subsidiary, the Western India Match Company (WIMCO) now produce more than two-thirds of the total production of matches in India. It owns and operates a large number of factories in Bombay, Calcutta, Madras, Punjab and U.P. In the cement industry, the biggest combination is the Associated Cement Co., Ltd., (A.C.C.), which was formed in 1936 by the amalgamation of 11 cement companies. Since then A.C.C. has set up three more factories. In all, A.C.C. controls 15 cement companies, and its rival, the Dalmia Group, controls 5 cement Companies.

Some combinations have also been formed by the amalgamation of managing agency firms, while the individual concerns under their management were allowed to retain their separate existence. This tendency became prominent after the Second World War. Thus the British India Corporation Ltd., a giant British managing agency firm. acquired in 1946 the business interest of Messrs. Beg Sutherland & Co.,

Ltd. leading to the concentration of management of 19 concerns. Similarly, in the same year, another two leading British managing agency firms, Jardine Skinner Ltd., and George Henderson & Co., combined to form one organisation in the name of Jardine Henderson Limited.

It must, however, be admitted that the growth of combinations has not yet proceeded so far as to secure a stronghold over the industries, except in the Match industry. The tendency is of course present, and has got to be watched carefully.

Monopolies Commission : In view of the complaints regarding the spread of the combination movement in the industrial sector, the government appointed a Monopolies Enquiry Commission in May 1964. The Commission issued its report in December, 1965. The Commission expressed the opinion that there was some amount of concentration of economic power in the industrial field. But it did not consider that it has as yet been of a character detrimental to the interests of the country. For the future it has suggested the passage of a legislation for the setting up of a statutory body for controlling and preventing the restrictive monopolistic malpractices. Wherever such a complaint is received from the government or from a director of investigation attached to the commission, the proposed Monopolies Commission is to conduct a judicial enquiry regarding the complaint, and if justified by the results of the enquiry, to issue an order to the monopolist to discontinue the practice complained of. It will also have the power to conduct from time to time an enquiry into the structure of any monopoly industry and to suggest appropriate measures to deal with the problem. No proposal for the amalgamation or merger of a big enterprise with another, or for the appointment of a person who is already a director of a big undertaking as the director of another undertaking engaged in the same line of business is to be carried out without the approval of the commission. It will also have the power to obtain annual returns from big companies to enable it to watch the operations of large concerns. Thus this statutory commission will act as a sort of watchdog to guard against the growth as well as the abuses of the monopoly in the Indian industrial sectors. The government is already taking steps for the establishment of such a commission.

Questions

1. How far is the existing location of industries satisfactory ? Do you advocate State control over the location of industries ?

2. Examine the case for the rationalisation of industries in India, laying adequate stress on the difficulties of such rationalisation.

3. Comment on the nature and extent of the combination movement in Indian industries.

CHAPTER 26 LABOUR SUPPLY AND EFFICIENCY

Throughout the whole of the 19th century organised industry suffered from a shortage of labour. This was due to a variety of factors. In that century growth of population was not very rapid, and the supply of land was not exhausted. Hence workers had to be attracted to the factories. Unfamiliarity with work in factories and the extremely unsatisfactory working conditions in factories,—all these were important factors in causing labour shortage. Moreover, certain industries like the tea plantations, coal mines etc., were situated far away from the usual centres of population, and these had to adopt special measures for the recruitment of labour.

Hence industries had to adopt special methods for securing an adequate supply of labour. Conditions have, of course, changed for the better for the vast majority of industries. The jute mills, the sugar and cotton mills, for example, are now able to get labour at the factory gates instead of sending men to the distant villages to bring recruits. But this change in the conditions of supply has not led to any significant change in the methods of recruitment of labour.

Methods of recruitment : Existing methods of recruitment exercise some influence on labour efficiency and welfare. This is due to the existence of certain peculiarities in these methods which will be obvious as we study them one by one.

The most usual method of recruitment is through a class of intermediaries known as the jobber, mistries or sardars. They are generally old workers promoted from the ranks after full experience in the factory. They recruit all labour required by the mill. Intending applicants have to approach them for a job, and their recommendation is also necessary for securing a promotion. Jobbers may also perform other functions, such as supervision of labourers at work, keeping the machinery in order etc.

This method of recruitment has led to many evils. It has led to much bribery and corruption as jobbers have to be paid something for securing, and also for retaining a job. This reduces the already low earnings of workers and so leads to lower efficiency. This method also leads to large labour turnover in our industries. The larger the labour

turnover, the larger the number of available jobs and so greater becomes the possibility of earning bribes. For these reasons the Royal Commission on Labour recommended the abolition of this system.

A second method of recruitment is through contractors. A factory needing workers looks to the contractors who supply the required number of labourer and receive commission for their services. This system prevails in railways, coal-mining and other mining industries etc. From the point of view of employers this system has the merit that it ensures a steady supply of labour and relieves the management of a lot of trouble regarding labour. But its distadvantages are more weighty and numerous than its merits. It enables employers to escape most of the provisions of labour legislation as contract labour is not directly employed by the factory. So the factory owner might disavow all responsibility for such workers. But the greatest defect is that this method leads to sweated labour. Contractors are mostly middlemen interested in making the maximum profit for themselves and this they do by overworking labour. A contractor for labour, chosen because he is the lowest tenderer, is also likely to pay the lowest rates of wages. There is no doubt that this system should also be given up as early as possible.

A third method is recruitment through labour officers. A large number of jute mills and other factories have appointed a number of labour officers in charge of a Labour Bureau for the recruitment of labour. This method has good potentialities, and can be used to eliminate the jobber and the contractor. But in many cases, especially in jute mills, these officers serve only as a screen behind which the system of recruitment by jobbers still continues.

Mention must also be made of the system followed in the Madura Mills Co., where the management sends notice of vacancies to the labour union. In some cases the management has started the practice of recruiting through the employment exchanges.

Employment exchanges : The Government of India started a number of employment exchanges mainly for the re-settlement of the demobilised personnel from the armed forces. The scope of activities of these exchanges has since been widened to include all classes of unemployed persons, and a number of private employers utilise the services of these exchanges for the recruitment of their staff.

There is a great need for extending the scope of operations of employment exchanges. The number of such exchanges should be increased and there should be at least one employment exchange in all industrial centres where representatives of employers and workers should be associated in an advisory capacity. Japan also suffered from similar difficulties regarding the recruitment of labour, and these were solved to a large extent by the organisation of employment exchanges.

The Shiva Rao Committee, appointed by the Government of India in 1952, issued a report in 1954 suggesting a plan for the reorganisation of employment exchanges. The Committee has rightly recommended that the employment exchange organisation should be developed into a full-fledged national service on a permanent footing with much enlarged powers. It recommended a wide range of functions for such exchanges, *viz.*, registration of all applicants, selecting and referring suitable applicants to employers and maintaining placement records, collecting information regarding employment opportunities and making such information available to workers etc. Government and semi-Government Departments should be required to recruit the required staff through these exchanges. As regards private employers, the Committee recommended that firms engaged on government contracts, concerns in which governments hold a part of the stock or grant subsidies or other aid should be required compulsorily to notify to the exchanges all vacancies other than vacancies of unskilled labour, temporary vacancies and promotions. The suggested measure of compulsion may be embodied in a suitable legislation with powers to the government to determine which particular categories of industries should be brought under the Act.

A competent organisation of employment exchanges is vital to successful economic development. Such an organisation can play an important part in assuring better employment of manpower resources and so in raising national productivity.

An Act has been passed providing for an enlargement of the scope of employment exchanges. In future, not only all employers in the public sector but those in the private sector would be required to notify all vacancies to the Employment Exchanges.

Efficiency of labour : That the average worker in India has a comparatively low efficiency has become one of the most common statements in economic writings. Labour efficiency is measured by the output per man-hour, *i.e.*, output which a worker produces on

average in one hour. Many attempts have been made from time to time to measure such efficiency as against that in some of the western countries, of course in every case to the disadvantage of the Indian worker. Thus one witness expressed his opinion before the Industrial Commission of 1918 that a cotton mill worker in Lancashire was about four times as efficient as his prototype in India. The Tariff Board on the Cotton Textile Industry, reporting in 1926-27, came to the conclusion that while a worker attended to 240 spindles in Japan, 5 to 6 hundred spindles in the U.K. and 1,120 spindles in the U.S.A., the Indian worker attended to only 180 spindles. Instances can be multiplied. The fact remains that on average, the Indian worker is less efficient than workers in industrially advanced countries.

What factors are responsible for such low efficiency? Certain causes are well-known, such as the climatic conditions of this country, the poor physique of the average worker and the prevalence of disease among them. Workers with their absurdly low standard of living have to live on an unsatisfactory diet in a thoroughly insanitary bustee. If the worker has to spend his night in a small room with wife and children, parents and other co-tenants all through the year, and in some cases cook his food there, he cannot get sound sleep or sufficient physical and mental rest as is necessary for one who has to put in hard and sustained physical work. How much of his physical and mental energy would, then, be left for efficient production in the factory?

A second group of factors have to do with the illiteracy of the average worker. Most of them lack any technical training. In other countries there are now industrial workers who can claim traditional skill in handling machinery etc., handed down to them through several generations, while in India only a small percentage of workers can claim such skill or technical training.

Some writers have also pointed attention to the migratory habits of the Indian worker and the high rate of labour turnover in the factories as being important causes of low efficiency. Most of the workers have migrated from the rural areas. They retain their link with the village homes and land and try to go back as often as they can to the villages. They are prone to look upon factory work as a disagreeable necessity, and so fail to strive to their utmost capacity for gaining efficiency. But such migration to the villages has also important beneficial effects. As the Royal Commission on Labour pointed out, the village home is a refuge

and security in sickness and in maternity, in strikes and in lockouts, in unemployment and in old age. An occasional visit to the village provides the worker with a cheap holiday in familiar surroundings and so improves his health. Hence migratory habit cannot always be regarded as a factor leading to inefficiency.

The Indian factory worker is supposed to have a fancy for changing the factory as often as he can. This and his migratory habit are responsible for the high rate of turnover of labour in the factories. If labourers frequently leave a factory, this causes great difficulties for the management who has, as a consequence, to select new employees most of whom may be inexperienced or completely new to the factory. They are likely to damage machines and materials. As a result, average productivity becomes smaller than would be the case with a constant labour force.

Two most important factors in high productivity of labour are the supply of good raw materials and the proper planning of production processes including the layout of the factory. Indian management is not always careful about the quality of raw materials to be used in the factory. Poor quality of raw materials leads to low output. Similarly the use of old, wornout machinery in many of the Indian factories is an important cause of low production.

Working conditions inside the factory itself and the degree of comfort provided for the worker also play a very large part in production. Such things as the percentage of humidity, the temperature, the lighting, spacing in the factory, the condition of the air and the amount of fibre or other materials floating in the air, noise and cleanliness in the factory etc.,—these are important factors in labour productivity. Such conditions as exist in most of the factories in India are also responsible for the low average output of the workers. The Indian worker alone is not to be held responsible for his low efficiency. He is often the victim of conditions over most of which he has no control.

Remedies: Once we know the factors responsible for low efficiency, it is comparatively easy to prescribe remedies. The housing conditions, the diet and medical facilities should be considerably improved. Greater provisions should be made to impart general and technical training to the workers, and the governments should start an increasingly large number of technical institutes. The institution of sickness insurance and provident fund schemes, and better housing are expected to lead to

a lower rate of turnover of labour. Above all, there is an imperative necessity for improving the efficiency of the management as a whole. The Development Councils should set up organisations to study productivity of labour and to suggest ways and means of improving it. If rationalisation is carried out carefully so as not to cause large-scale unemployment, productivity of labour is likely to increase in the long run.

Productivity of labour in recent times : One of the most frequent complaints heard is that the average productivity of labour has declined materially over the post-war years. For example, the Chairman of the Tata Iron & Steel Co., has stated in his annual report of 1949 that the average output of steel per worker has declined from 24·36 tons in 1939-40 to 16·30 tons in 1948-49. In the coal industry, while the number of workers employed during the decade ending 1951 has gone up by 58 p.c., output has increased by only 32 p.c. In the Cotton Textile Industry, the Planning Commission estimated that productivity had generally declined by 20 to 30 per cent during the period following the Second World War. This has happened at a time when productivity has increased in such countries like the U.K., the U.S.A., and Japan, India's chief competitors. This if true, must be one of the most disquieting features in our industrial development.

A study of the changes in the productivity and earnings has been made in a number of industries in 1955, and the results show the following interesting facts : In the cotton textile industry, the average productivity of labour has risen by 2·28 p.c. per year between 1948 to 1953 as against a rise of 1·14 p.c. in earnings. In the jute industry, productivity has risen during the same period by 2·9 p.c. as against 3·7 p.c. in earnings. In the paper industry, there was no evidence of any increase in productivity while earnings rose. In coal-mines, earnings rose by only 0·26 p.c. as against 0·76 p.c. in productivity.

Various factors have been stated to have caused such a decline. These are (1) the prevalence of indiscipline among workers, (2) the inability of the employer to exercise the right to discharge labour on account of the operation of the Industrial Disputes Act, (3) the "go-slow" tactics adopted deliberately by labour to increase the volume of employment, or to force employers to come to terms, (4) the rise in wages and dearness allowances making it easy for the workers to maintain their low standard of living etc. There is no doubt that part of

the decline in productivity must be ascribed to the aging of the machinery and other equipment and the difficulties of securing raw materials of good quality in some of the industries. Whatever the truth of the analysis, time has come for all parties to get together and devise proper measures for increasing the productivity of labour in different industries.

Questions

1. Discuss the causes of inefficiency of industrial labour in India. Indicate the lines of reform you would suggest.

2. Examine the different systems for the recruitment of labour in India. Describe the part played by employment exchanges in this connection.

3. Do you think that the productivity of labour has declined in recent years ? How do you account for such a decline in productivity ?

CHAPTER 27

PROBLEM OF MINIMUM WAGES AND SOCIAL SECURITY

Fixation of minimum wages : In almost every industrialised country the government had to take up the task of fixing minimum wages for special groups of labour, such as those who are in receipt of specially low wages or who are unorganised. The same conditions are also present in India. In this country, most of the workers received very low wages in a large number of industries. They are mostly unorganised. Trade unions have of course been established. But most of these unions are comparatively loose organisations, and habits of collective bargaining have not been developed. Hence the state in India was forced to intervene in a large number of cases and fix minimum wages for different groups of labour.

Proposals for setting up a machinery for fixing minimum wages were before the Government of India from a long time. The government was asked in 1926 to ratify the ILO convention on the fixation of minimum wages. But it did not consider it practicable to ratify the convention. The Royal Commission on Labour did not also consider it to be a practicable proposition mainly on the ground that we did not possess any statistics showing the extent to which labourers received "sweated" wages. The Commission, however, was inclined to favour the proposal for setting up a wage board for fixing minimum wages in the tea plantations of Assam. A number of Labour Enquiry Committees gave a favourable consideration to the proposal for fixing minimum wages. Nothing was, however, done by the government before the end of the Second World War.

At the present moment minimum wages have been fixed in almost all the large-scale industries and in a number of medium-sized and small-scale industries. This has been done under two different Acts, *viz.*, the Industrial Disputes Act (1947) and the Minimum Wages Act (1948). The former set up a machinery in the form of Industrial Tribunals for the settlement of industrial disputes. As the vast majority of these disputes were concerned with the question of wage rates, these Tribunals had to take upon themselves the task of fixing minimum wages. These Tribunals fixed minimum wages in almost all the major industries.

Minimum Wages Act: The Minimum Wages Act (1948) was passed for fixing minimum wages in certain selected industries, where workers were in receipt of exceptionally low wages on account of the lack of or weaknesses of the trade union organisations. The provisions of this Act are applicable to industries like tea plantations, oil mills, rice mills, flour mills, motor transport, tanneries etc., and agriculture, which have been mentioned in the schedules. Excepting the plantations and agriculture, all others are minor industries. The State Governments have, however, the power to add to the list of industries. No minimum wages are to be fixed in an industry which employs less than 1,000 workers. In agriculture, minimum wages are to be fixed within 3 years; in all other industries within 2 years. The period has, however, been extended by subsequent amendments.

The Act lays down the following machinery for fixing minimum wages. The State Government may itself publish proposals for fixing minimum wage rates in an industry; or it may appoint a committee to hold enquiries and suggest minimum wage rates. These are then to be published in the Gazette and shall come into force at the end of 3 months. Wage rates so fixed are to remain in force for not more than 5 years after which they are to be revised. Before any revision is to be made, the Government shall appoint Advisory Committees to advise it on the extent of revision. For the purpose of co-ordinating the work of these Committees, the State Government shall set up an Advisory Board. The Central Government may also set up a Central Advisory Board for advising the State and Central Governments in matters of fixation and revision of minimum wage rates. All these Committees and Boards are to consist of an equal number of representatives of employers and workers of each industry, and a number of independent members (not exceeding one-third of the total number of members). All members are to be appointed by the government which shall also select one of the independent members as the Chairman.

The government may fix minimum wages for time or piece-work. It may also fix different minimum rates for adults, women, children and apprentices or for different classes of work or for different localities. A minimum wages rate may consist of a basic rate with or without a cost-of-living allowance, and may be fixed in cash or kind. The Act has not laid down any principles for fixing minimum wages.

The scope of the Act is of course restricted. It does not apply to any large-scale industry with the exception of plantations, and it

excludes industries employing less than 100 workers. So it is applicable only to minor medium-sized and small industries. Moreover, fixation of minimum wages by a government department is not a desirable proposition. The appointment of a wage board in the form of an Advisory Committee ought to have been made obligatory in all cases. Recently the Central Government has set up Wage Boards for cotton textiles, cement and sugar industries.

Principles for fixing minimum wages : What principles have generally been followed in fixing minimum wages ? Those who demand the fixation of minimum wages want such wages to be determined on the basis of ensuring a "living wage" for the workers. This is known as the principle of living wage. The principle of living wage, according to which wages should be equal to "a sum sufficient for the normal and reasonable needs of the average worker with an average family in the locality" represents a widespread popular aspiration.

While the principle looks reasonable at first sight, difficulties arise with regard to its practical application. What, exactly, constitutes "the normal and reasonable needs" of a worker ? Different people will have different ideas on this point. Who is an average worker ? What is the size of an average working class family ? What of those workers who have a large family or have to support old parents or other relations ? In practice, therefore, most of the authorities have refused to declare a living wages differing in any marked degree from the current ruling rates.

Another principle that is often stressed, especially by employers, is the capacity of the industry to pay. Hence also difficulties arise with regard to the determination of the capacity of the industry to pay. Are we to measure the capacity of an industry to pay in the short period ? Or in the long period after allowing for expansion and modernisation ? The rates of profit earned by the industry are not a good guide as balancesheets can be, and have been, manipulated.

In view of these difficulties reliance has been placed in fixing minimum wages on existing rates paid by the best employers in the industry or in comparable occupations. The Trade Boards in the U.K. often paid great attention to this factor. Sometimes general economic considerations, such as the prevalence of depression or prosperity in the industry or in the country have also been taken into account.

Reliance on any single formula is not possible. In practice the authorities in different countries have taken into account a variety of principles. The precise weight to be given to each of these principles has varied at different periods and countries.

In India, the most important factor in fixing minimum wages has been the Report of the Central Pay Commission (1947). After expressing its conviction that the State must take some step towards fixing minimum wages on the basis of the principle of living wage, the Commission, however, felt that this might not be possible in the initial stages. So as a first step it sought to fix minimum wages related to the normal wage level prevailing in the country. The Commission recommended a minimum basic wage of Rs. 30 per month. This report constitutes as a landmark as the principles and practices recommended in it came to be accepted as authoritative by almost all subsequent adjudicators.

Adjudicators have also sought to pay attention to the principle of the capacity of the industry to pay. But this has been done, more or less, for the purpose of ascertaining whether the wages recommended by them on other considerations were within the capacity of the industry or the industrial concern. This principle formed mainly an indirect test as to the possibility of a certain wage recommended rather than a positive factor deciding the actual level at which to fix wages.

Other factors have only been touched lightly in the awards of the different tribunals.

The various Committees set up under the Minimum Wages Act have also emphasised the first two principles. Most of them have adopted the definition given by the Fair Wages Committee that "the minimum wages must provide not merely for the bare sustenance of life, but also for the preservation of the efficiency of the worker, by providing some measure of education, medical requirements and amenities." But as the minimum wage determined on this basis was beyond the financial capacity of these industries it has to be scaled down. In practice, therefore, the legal minimum was fixed at as high a point as the industry could hope to bear in normal times.

Effects of fixation of minimum wages : The most usual criticism made against the fixation of minimum wages is that it would raise costs and so hamper industrial development. If minimum wages are

fixed at high levels, employers would dismiss those workers who were not worth such wages. As a result. unemployment would increase.

Much will, of course, depend on the level at which minimum wages are fixed. If the second principle (capacity of industry to pay) is given due weight, no adverse effect would follow the fixation of minimum wages. If the first principle is followed rightly, the effects would depend on the gap between existing wages rates and the living wages. In practice, while lip service has been paid to the principle of living wages, its application in India has been tempered by many considerations.

Moreover, regard must be paid to the effects of higher wages on the efficiency of the workers. Higher wages would lead to better standard of living and so stimulate workers to increase output. It would also force employers to exert themselves to a greater extent and to make various improvements in their factories. Against this contention it has been urged that in India the general tendency has been that a rise in wages is usually followed by increased absenteeism among workers. In so far as this happens, productivity of workers would not increase. But while this may be the fact in individual cases, such effects were more likely to be temporary. On the other hand. the scope for improvements in efficiency is likely to be greater in view of the low standard of living of the workers.

Fair wages : While minimum wages have been fixed in different industries, this was not considered enough, and the Industrial Truce Resolution of 1917 advocated the payment of fair wages to labour as essential for the maintenance of industrial peace. In pursuance of this resolution. a Fair Wages Committee was appointed in 1948 and issued its report next year. A Fair Wages Bill was introduced in the Parliament in 1953. But it was subsequently allowed to lapse.

The Fair Wages Committee, and following its recommendation, the Bill made a distinction between a minimum wage, a fair wage and a living wage. The minimum wage must provide not merely for the bare sustenance of life but for the preservation of the efficiency of the worker by providing for some measure of education, medical requirements and amenities. It is the absolute minimum below which wages should not be allowed to fall. A "living wage" represents, on the other hand, a standard of living which provides not merely for a bare physical sustenance but for the mainteance of health and decency, a measure of frugal comfort and some insurance against the more important

misfortunes of life. While the attainment of a living wage is the direct objective of every civilised state, it may not be possible to act on this principle in India where the national income is very low. Hence we have to fall back upon a compromise, *i.e.*, the principle of fair wages. A fair wage is generally higher than a minimum wage, but lower than a living wage. Its level is to be determined by taking into account the capacity of the industry to pay, the level of national income, the prevailing rates of wages and the productivity of labour etc.

The Bill provided for the setting up of a Board for determining fair wages. The Board should determine fair wages on an industry-cum-region basis and should take due note of all relevant factors. The level of fair wages should be so fixed as to enable industry to maintain production with efficiency. It should not go out of line with wages in other industries as to cause movement of labour and consequent industrial unrest.

Sickness Insurance: In western and other industrialised countries governments have adopted the policy of insuring workers against the expenses made necessary by sickness. In return for a small weekly or monthly payment deducted from their wages, workers are given free medical treatment and cash payments during periods of sickness. Compulsory sickness insurance for industrial workers was first introduced in Germany in 1883 and in the U.K. in 1911. By 1936, 31 countries had adopted such schemes.

The necessity for adopting such a scheme in India is admitted by everybody. The worker in India receives very low wages and has, therefore, no or very small savings. As he cannot go to the factory during periods of sickness, he does not receive any wages at a time when, in addition to his usual expenses, he has to pay for his medical treatment. Hence a large percentage of workers cannot afford to have any medical treatment, and their health and efficiency suffer as a consequence. All of them have to incur debts during such periods to defray their usual expenses. A scheme of compulsory sickness insurance would provide free medical treatment and cash payments to workers during their sickness and so improve their health and efficiency. Recognising this, a number of good employers like the Tata Iron & Steel

Co., the Angus Jute Mills etc., have started hospitals and are providing free medical treatment for their workers. Some of them also grant sick leave with full pay for a number of days. But this benefit is enjoyed by only a small percentage of workers.

The proposal for introducing a compulsory sickness insurance for the industrial workers came before the Government of India in 1928. The Government decided not to adopt the scheme in view of the fact that it did not possess statistics of the incidence of sickness among industrial workers. The Royal Commission on Labour recognised this difficulty; but it recommended that in order to get some idea of the probable cost of such a scheme, the government might introduce a tentative scheme applicable to a single establishment. Nothing was, however, done on this point. During the Second World War, the government at last felt compelled to consider the proposal and appointed Prof. B. P. Adarkar to submit a report on the scheme of sickness insurance. He submitted his report in 1944 in which he forwarded a scheme.

Prof. Adarkar's scheme was examined by two experts from the ILO, who suggested that the scheme of sickness insurance should be integrated with workmen's compensation and maternity benefits. A Bill embodying the conclusions of the government was introduced in the Parliament and finally passed in 1948 under the name of Employees' State Insurance Act.

Employees' State Insurance Act. This Act provides for sickness, maternity, disablement and dependents' benefit for all industrial workers. All workers employed in factories employing 20 or more persons and using power will be brought within the operations of the Act, and the governments have the power to extend the scheme to other establishments. Employees whose remuneration exceeds Rs. 400 a month are to be excluded from the operation of the Act. Seasonal factories are also to be excluded.

All workers who are to be insured under the Act will pay contributions at rates depending on their remuneration. The following table shows the rates to be paid by workers and employers per month.

Class of Employees	Employee's share Rs. P.	Employer's share Rs. P.	Total Rs. P.
(a) Those whose daily wages are below Re. 1/-	Nil	0 44	0 44
(b) Those receiving between Re. 1 and Rs. 1/50 per day ..	0 12	0 44	0 56
(c) Those receiving between Rs. 1/50 and Rs. 2	0 25	0 50	0 75
(d) Those receiving betwen Rs. 2 and Rs 3	0 37	0 75	1 12
(e) Those receiving between Rs. 3 and Rs. 4	0 50	1 00	1 50
(f) Those receiving between Rs. 4 and Rs. 6	0 68	1 37	2 06
(g) Those receiving between Rs. 6 and Rs. 8	0 94	1 87	2 81
(h) Those receiving between Rs. 8 and above	1 25	2 50	3 75

In return for these payments, workers will receive the following benefits. (1) Free medical treatment from the first day of sickness. The authorities may at their discretion extend this benefit to the family of the worker (*i.e.*, wife. minor children and dependent parents). (2) Cash payments from the third and successive days of sickness at the rate of one-half of the average assumed daily wages. No cash will be paid for the first two days of sickness. Such payments are to be continued in cases of prolonged or frequent sickness up to a total of 56 days during a period of 365 days. But before a worker can claim cash payments, he must have paid contributions for a period of 6 months or two-thirds of the contribution period with a minimum of 12 weeks. (3) Disablement benefit. Workers who have been disabled through employment injury either partially or totally will receive free medical treatment plus cash payments. Dependents of a worker who has died from employment injury will be paid pensions at rates prescribed in the Act. (4) Maternity benefit. Women workers will receive cash payments at the rate of 75 P. per day during a period of 12 weeks of which not more than six shall precede the expected date of confinement.

The scheme is to be administered by a Corporation called the Employees' State Insurance Corporation consisting of 31 members with the Central Minister for Labour as the Chairman. The different State Governments will nominate representatives and the Central Government

will also nominate 5 representatives each of the employers and employees, in consultation with their organisations. The Parliament will also nominate two representatives. The Corporation will have a small Standing Committee of 13 members, and there will be a Director-General appointed by the Central Government to act as the chief executive officer of the Corporation. The Corporation is to receive a grant from the Central Government for the first 5 years.

Provisions for medical treatment are to be made by the State Governments with the agreement of the Corporation, which shall share the cost with the governments.

As the government found it difficult to put the scheme into operation simultaneously in all parts of the country, it was decided to carry it out in different areas according to a fixed time table. Thus it was first started in Delhi and Kanpur in February 1952, to be extended to Punjab in August 1952, followed by Greater Bombay and Bangalore in January 1953, and Madras, Calcutta, Nagpur and Jubbalpore in January, 1955. It now covers about 1·7 million employees to whom 7 lakhs more were added in 1961-62. When the scheme was sought to be introduced in Delhi and Kanpur, employers protested on the ground that the payments they would have to make under the Act would raise their costs and so would place them at a disadvantage with employers in other parts of the country. The Act was, therefore, amended in September 1951 authorising the government to ask employers in all parts of the country to make payments even if the scheme was not introduced in their areas.

The scheme unfortunately encountered considerable opposition from its inception. Opposition came mainly from the side of the workers. In areas where the scheme had been put into operation, some of the employers had been in the practice of providing excellent medical facilities to workers and their families who were not required to pay any contribution in return. Secondly, the scheme in the initial stages did not propose to provide medical treatment for the families of the insured workers. As a result, these groups of workers opposed the introduction of the scheme which forced them to pay for benefits which they were enjoying free of cost. Moreover, no special arrangements were made at Kanpur and Delhi for the hospitalisation of the workers who had, however, to make contributions. Unless more hospital facilities were provided at the same time on or near the factory premises,

the scheme will not naturally be popular among the workers. Recently, the benefits of the scheme have been extended to the members of the families of the insured workers, and the employers' contribution have been raised from 1·25 p.c. to 2·50 p.c. of their wage bill.

Employees' Provident Fund Act : The necessity for introducing the system of old age pensions was pointed out by two members of the Royal Commission on Labour. (Mr. N. M. Joshi and Diwan Chaman-lall). Industrial life tends to break down the joint family system on which old people rely for their maintenance. The vast majority of workers receive so low wages that they cannot save much for their old age. Hence workers have to pass a very miserable life in their old age.

Some provisions for old age existed in a few industries in our country. The railways, some government departments, a few cotton mills in Bombay and other places adopted a scheme of contributory provident fund. Workers regularly contributed, either on a compulsory or voluntary basis, a certain percentage (generally 6¼ p.c.) of their wages or salaries, and the employers contributed an equal amount. A few factories paid gratuities, while the payment of pensions was rather rare.

These schemes covered only a small percentage of the workers. Even in those industries where they were adopted, the scheme generally excluded the low-paid staff, where the need was the most urgent. These schemes were unsatisfactory for another reason. There was an absence of any set of rules, and everything depended on the decision of the management, which might not always go in favour of the workers.

A scheme for the introduction of provident funds on a compulsory basis was first introduced by the Government of India in the coal mines. It was later extended to other industries by the Employees' Provident Fund Ordinance promulgated in November, 1951. The Ordinance was in due course replaced by an Act.

Under the Employees' Provident Fund Act, the provisions were originally to apply to six groups of industries, *e.g.*, cement, cigarette, engineering, iron and steel, paper, and textile industries (cotton, jute and silk). Its scope has later been increased to 41 industries. By the end of October, 1961, 16281 establishments covering 30·75 lakhs employees have been brought within the scheme. All establishments in these industries which are more than 3 years' old and which employ more than 50 workers were to be brought under the scheme. New

concerns were to be exempted from these provisions for a period of 3 years. Provident fund deductions are to be made from the wages of all workers at the rate of $6\frac{1}{4}$ p.c.*. In calculating contributions both the basic wages and dearness allowances are to be taken into account. The employers are to contribute an equal amount and to bear the cost of administration of the Fund. The government may allow any group of workers to pay contributions at higher rates. The money thus realised was to be invested in Government securities. Facilities are to be provided for members for the payment of insurance premia out of their own contributions to the Fund. If old employees of 10 years' standing in a concern operating such a scheme consider that the existing pension or gratuity benefits are better, they would have the option of remaining in the old scheme.

The provisions of this Act have been criticised on the ground that they are likely to put a great strain on the finances of industrial concerns. Employer's contributions are clearly an addition to wages and so would raise costs. But the adoption of such a scheme is likely to react favourably on the efficiency of the workers, it is also likely to reduce the rate of migration of workers from factory to villages or from factory to factory. These are factors likely to reduce costs. But it must be admitted that as the scheme provides for old age, it is a sound measure of social security. Moreover, it forces workers with low incomes to save at least something out of their earnings. These people would not have saved anything in the absence of such compulsory provisions. These savings would be available for investment purposes. So this scheme has the undoubted merit of accelerating capital formation.

The Provident Fund scheme has been amended in 1960 to allow the Central Provident Fund Commissioner to grant advances to members of the Fund for the purchase of a dwelling house or site, construction of a house etc. The advances are to be made out of the own contributions of the members and shall not exceed their 12 months' basic wage or their own contributions whichever is less. Such advances are to be granted only to those members who have paid their contributions for at least 10 years (7 years in some special cases).

* The Government proposed to raise this percentage to $8^1/_3$, and as this has been opposed by the employers, a committee have been appointed to consider the question of the capacity of the industries concerned to pay the increased contribution. (21-5-60).

Social security for workers : In the more advanced countries, the State had taken a number of measures for providing security to the industrial workers against the risks of sickness, accident, death and other ailments. A comprehensive scheme providing for free medical treatment and the payment of adequate cash benefits during sickness. payment of proper compensation for industrial accidents. payment of old age pensions and of unemployment benefits etc. is known as the social security system. The objective of such a scheme is to assure the workers of the certainty of the maintenance of a minimum standard of living during all such hazards like sickness, old age, unemployment, death etc.

As is quite obvious, such a system of social security has only been partially introduced in our country, and it covers more or less the workers engaged permanently in perennial factories. The State in India has introduced the sickness insurance scheme, which seeks to provide for free medical treatment and for the payment of some cash benefits during the period of sickness, the payment of compensation for industrial accidents. and of maternity benefits. There is no provision for the payment of old age pesnsions. though the introduction of the Provident Fund Schemes in a number of industries acts as a partial substitute for such pensions. The workers have at least been assured that if they worked for a stated number of years, they would have something to fall back upon after their retirement. There is as yet no provision for the introduction of unemployment relief. for the payment of any other benefits to the workers.

The main difficulty standing in the way of the adoption of a full fledged scheme of social security is of course the lack of funds. This is possible only when the national income of the country is sufficiently high to bear the burden of financing such a scheme of comprehensive social security. This is the inevitable dilemma of a poor country. The poorer a country is, the greater is its need for providing social security to the people, and the greater is the difficulty of adopting such a scheme.

Questions

1. Discuss the reasons for fixing minimum wages in India, and examine the effects of fixation of minimum wages.

2. Examine the main provisions of the Minimum Wages Act of 1948. What principles have been followed in fixing minimum wages in India ?

3. Describe the problem of a fair wage rate in any organised industry.

4. Examine the necessity for introducing a scheme of sickness insurance in India. Discuss the main provisions of the Employees' State Insurance Act.

5. Discuss the provisions of the Employees' Provident Fund Act and examine its effects on Indian industry.

CHAPTER 28

TRADE UNIONS AND INDUSTRIAL RELATIONS

Trade union movement : Though industrialisation on modern lines is now more than a century old in India, the development of trade unions came much later. The credit for establishing the first organisation of workers in this country goes to Mr. Lokhande of Bombay who organised the Bombay Millhands Association in 1890 and presented a memorial to the Government on the eve of the passage of the Factory Act. This was, however, a loose and extremely short-lived organisation. In 1897 the Amalgamated Society of Railway Servants of India and Burma was formed mainly for benevolent purposes. Attempts were also made in a few cases to establish unions in the years before the first world war. But these were ineffective.

The real growth of the movement came after the first world war. That was caused prices and costs of living to rise to high levels, while wages everywhere lagged behind. This led to the emergence of much discontent among workers, who were emboldened by the rise of Communism in Soviet Russia. The political movement was gathering momentum, and the leaders wanted to broaden the base of the movement by forming organisations among the industrial workers. The result of all these factors was the rise of the trade union movement.

The first trade union was organised in Madras by Mr. Wadia in 1918. One by one other industrial areas followed suit and a large number of unions came into existence within the next few years. But these unions were mostly strike committees without any solid foundation. These unions were isolated organisations and soon attempts were made to set up an institution to co-ordinate their activities. This need was followed by the organisation of the All-India Trade Union Congress in 1920. It was a national federation of unions. This federal organisation has a chequered history behind it. In 1928-29 this organisation was captured by the Communists and other left-wing leaders, and the moderate element formed the All-India Trade Union Federation under N. M. Joshi. This split and the prosecution of left-wing leaders in the famous Meerut Trial weakened the movement. Efforts to arrive at a compromise were made and finally a provisional agreement uniting the two groups were reached in 1940. The outbreak of the second world

war led to further dissensions and while the main body, the Trade Union Congress, favoured a policy of neutrality, another group under Mr. M. N. Roy seceded and formed the Trade Union Federation with the policy of an all-out support to the war effort.

With the end of the war, labour leaders with strong Congress leanings formed another federal organisation in the name of the All-India National Trade Union Congress (INTUC) mainly with a view to counteracting communist influences among the workers. Later on, Socialists who formally seceded from the Indian National Congress, started their own federal organisation, called the Hind Mazdoor Sabha. A section of moderate labour leaders have also started another federal organisation in the name of the United Trade Union Congress.

Present position of the movement. The trade union movement has made remarkable progress in the last 25 years. The number of registered unions increased from 29 in 1927-28 with a membership of a little more than a lakh workers to 10,045 in 1958-59 with a membership of more than 30·57 lakh workers. There has been a rapid increase in the number of unions in the recent years after 1945, when the movement spread to many new industries and embraced "white-collar" workers (*i.e.* clerks and others) among its membership. There has also taken place a gradual increase in the number of women worker members, the percentage of women members to total membership rising from 1·5 p.c. in 1927-32 to 6·6 p.c. in 1949-50. Among industries, the largest number of unions have been organised in the cotton textile industry followed by banking and insurance, electricity, gas, water and sanitary services, railways etc. The three industrially advanced States of West Bengal, Bombay and U.P. contained about 64 p.c. of unions submitting returns and 68 p.c. of the reported membership. In general, the average size of trade unions is comparatively small. Unions with membership below 300 constituted nearly 59 p.c. of the total, and there is also a fairly large number of unions with membership below 50. Another disquieting feature is that a very small proportion of the funds of unions was spent on the ameliorative activities like the payment of compensation and benefits in cash and kind to the members.

Legal position of unions. When the first trade unions were started from 1918, there was no special legislation governing the rights and duties of unions. Following a case in the Madras High Court against the Madras Labour Union for inducing the workers to go on strike, there

was some agitation in the country for the protection of the rights of trade unions. The necessary legislation was passed in 1926, and the Indian Trade Union Act of that year as subsequently amended still governs the legal position of unions in this country.

Under that Act, any trade union (including organisations of employers) can apply for registration provided that it fulfils certain conditions. It must have a definite constitution and at least 50 p.c. of the members of the executive committee must be employed in the industry. A registered union has certain rights and obligations. First, it has to submit annual returns of its accounts to the Registrar with duly audited statements of its receipts and expenditure. Secondly, it can utilise its funds for certain general purposes laid down in the Act. Thirdly, it cannot utilise its general funds to further political purposes. But it may constitute a separate fund for political purposes to which subscription must be on a voluntary basis. In return for these obligations, it enjoys immunity against civil and criminal proceedings in respect of actions connected with the furtherance of a trade dispute.

This Act was amended in 1948. This provided for the compulsory recognition of a trade union by the employers. If a trade union fulfils certain conditions, it may approach the employer for recognition, and on his refusal. may approach the Labour Court to be set up for this purpose. To obtain recognition the Union must be registered under the Act ; all its members must be regular workers in the industry ; and its rules must not debar any worker from becoming its members ; and it is a representative body of the workers working in the industry or establishment. Its constitution must also contain a definite procedure for calling a strike, and it must not take part in an illegal strike. If the Labour Court finds that the Union satisfies the conditions, it will issue a certificate of compulsory recognition to the Union, which will then enjoy the right to negotiate with the employer in all industrial matters.

There is now a clear need for a revised, comprehensive trade union law. The Act of 1926 is defective on many grounds. It creates an anomalous position as it allows an employers' organisation to be regarded as a trade union. The Royal Commission on Labour made a number of recommendations for amending the Trade Union Act. It wanted that the expenses of conducting audit should be borne by the government, and that the proportion of workers in the executive of

the union should be raised to two-thirds instead of one-half as at present ; and that the unions should be allowed to start and operate funds for political purposes without any restrictions. Lastly, it advocated that the unions should be allowed to start co-operative organisations of their own.

Compulsory recognition of trade unions : We must also squarely face the need for the compulsory recognition of unions by law. Collective bargaining habits have not developed to the desirable extent on account mainly of the opposition and unsympathetic attitude of the employers. Though the Royal Commission on Labour exhorted the employers to adopt a more sympathetic attitude and negotiate with the unions on equal terms, very few employers have actually followed this advice. Time has, therefore, come for the State to step in and provide for the compulsory recognition of trade unions.

The law should, therefore, lay it down that if a trade union is well-organised and satisfied the conditions laid down in the Act, it should be granted a certificate. The employers would then be required to give recognition to such a union and conduct collective bargaining negotiations regarding wages and other conditions of work.

It has, however, been urged that such a provision for the compulsory recognition of a Union will ensure neither good industrial relations, nor the development of collective bargaining. If the employer is unsympathetic, no law can force him to conduct negotiations with union leaders. On the other hand, he may attempt to start what is known as a "company union" *i.e.* a union composed of workers whom he favours, and set it up as a rival to fight a real union. The development of collective bargaining is a matter of the mutual recognition of the strength of each other, and this, it is urged, can only be fostered gradually.

Trade Unions Bill of 1950 : In 1950, the government introduced a Bill in the Parliament dealing with the rights and duties of trade unions. The Bill has been allowed to lapse. In view of the importance of its provisions we propose to study its main points.

The Bill provided for the organisation and registration of a union. A trade union might be formed by any ten or more persons and may apply for registration. Registration was to be granted if it satisfies the following conditions, in addition to those laid down in the Act of 1926, *viz.*, its rules should provide for the payment of subscription by

ordinary members at not less than 2 as. per month, except that in the case of workers employed in agriculture, cottage industries etc., the rate might be lower : (*b*) the number of outsiders in the executive union were not to exceed 4 or one-fourth of the total number, whichever was less etc. A union consisting wholly or partly of civil servants could not appoint any outsider as an office-bearer, nor could it participate, directly or indirectly, in any form of political activity.

A registered union would have to maintain a list of members and a register showing particulars of subscriptions paid etc.; it must submit annual statements of accounts to the Registrar ; it must spend its general funds only on specific purposes recognised in the Bill, and it must not commit unfair labour practices (*i.e.* take part in an illegal strike etc.). In return, it was to enjoy immunity in civil and criminal proceedings and to maintain a separate fund for political purposes on an entirely voluntary basis and enter into collective bargaining with employers.

The Bill also provided for the compulsory recognition of unions almost on the lines as in the amending Act of 1948. If a registered union was refused recognition by the employer, it was to apply to the Labour Court. That Court was to issue a certificate of recognition provided that the union satisfied the following conditions, *viz.*, it was representative of all the employees. that its rules did not provide for the exclusion of any employee from membership on grounds of sex or religion or caste; that its rule included a procedure for declaring strikes ; and that its rules provided that meeting of the executive committee must be held at least once in 6 months.

The Bill came in for a good deal of criticism. The provisions relating to the formation of unions by civil servants, and those regulating the number of outsiders in the executive of the union were felt to be unduly restrictive. The Bill retained the provisions relating to the keeping of a separate political fund to be found in the old Act. Even the Royal Commission on Labour felt compelled to recommend the withdrawal of any restriction on the keeping of funds for political purposes. Lastly, while a trade union was asked to satisfy rather onerous conditions before it was to be granted the certificate of compulsory recognition, it was not granted any important rights in return. The only right conferred on a recognised union was to receive replies to its letters and to have interviews with employers. In addition, it should have

permission to collect subscriptions from its members and to hold meetings on the premises of the factory and similar other privileges.

Strength and weakness of the movement : In the last decade remarkable changes have taken place in the trade union movement. In the early stages the most of the unions were mere strike committees, which were organised on the eve of a strike, and faded away at the end of the strike. But at present the majority of the unions are more permanent organisations. They are better organised and the more active in many directions. They have wrested important benefits for the members and have fought a number of successful strikes. They have thus gained in self-confidence. Some of them like the Ahmedabad Textile Labour Union are rendering valuable services to their members through the establishment of schools, hospitals etc. The movement is now well-entrenched and has proved to be an important influence in the country.

But the movement exhibits several weak features. Though most of the unions are much better than strike committees, they are still now comparatively weak in organisation. Their membership figures are often inaccurate as subscriptions are irregularly paid. As unpaid subscriptions figure largely, their financial conditions are seldom very strong. As a result, very few of them can afford to pay strike benefits or unemployment and sickness benefits to their members. The welfare side of their activities has been very little developed except in the case of a few unions. In western countries labour welfare is regarded as one of the most important functions of a trade union. Trade unionism is not made at mass meetings or by fiery speeches alone. It grows out of the good earth of mutual service rendered.

Another serious weakness lies in the fact that as yet the majority of labour leaders have come from outside the labour ranks. These "outsiders" have of course rendered valuable services to the cause of the movement. But in order that the movement may be placed on a sound basis, its leadership must spring up from within the workers. The position has improved to some extent in recent years. Several leaders have sprung up from the working classes, and the educated people have been forced to join the factories for want of alternative occupations, thus providing the basis for the training up of leaders.

It must, however, be recognised that the organisers of the Trade Union Movement have to face certain difficulties. In the first place,

the average Indian labourer is illiterate and migratory in his habits. Lack of education often prevents workers from taking a long view of the situation ; and those who are frequently changing their factories or leaving for their village homes are not much inclined to maintain any permanent interest in any trade union organisation. The illiteracy of the average worker is also responsible for the dearth of labour leaders, as a result of which the movement has come to be led by "outsiders". Another serious handicap arises from the diversity of races, languages and religion to be found among the workers. They come from different States, talk different languages and follow different religious and social customs. It is not an easy task to organise such a heterogenous mass of people into one organisation. Employers have often exploited provincial or religious sentiments to thwart the organisation of a union. A third handicap has been the extreme poverty of the majority of the workers. It is, of course, true that in recent years money wages have been increased. But the cost of living has also risen high. To a large number of workers even a small subscription means some burden. Those whose wages are barely adequate for sustained activity are not likely to possess the energy required for taking an active interest in trade union matters. Unless subscriptions come in regularly and members take an active interest, no trade union can work successfully.

Industrial disputes

The maintenance of industrial peace is essential if production is to continue uninterrupted. Such peace is, however, often broken by the occurrence of disputes. Industrial disputes may take two forms, *viz.*, strikes and lockouts. Strikes are concerted withdrawal of all or a section of workers from work in an establishment with a view to force employers to come to terms with the workers. Lockouts mean the closure of a factory by the employers to force workers to submit to his orders. Usually strikes are more numerous than lockouts, and that is the reason why attention is focussed mainly on strikes while discussing industrial peace or industrial relations. It should, however, be noted that industrial unrest among workers may not always lead to a strike. It may result in the adoption of other policies like "go slow" tactics, increased absenteeism etc.

Before the end of the First World War, strikes were rather infrequent in Indian industries. Workers were unorganised and so

were unable to combine for the purpose of a strike. The rise of prices and cost of living uncompensated by any increase in wages, the organisation of trade unions and the spread of mass-consciousness among the workers led to a series of strikes in the winter of 1920-21. Since 1921 government has started publishing statistics about strikes. From 1929 the Government of India began to take steps for the prevention and settlement of strikes.

Causes of strikes. The causes that have led to strikes are of a diverse character, though it is possible to find out the more important ones among them. (*a*) The most important and the most frequent cause is the demand for the payment of higher wages and dearness allowances. Until recently the basic wage rates were extremely low in most of the industries in India, while the war-time inflation caused the cost of living to rise to high levels. In some cases dearness allowances were granted. But these were clearly insufficient to neutralise the rise in the cost of living. The demand for increases in wages and dearness allowances is thus the most important single cause of strikes. (*b*) Refusal to work long hours, and the demand for rest intervals, holdings etc., have also provided some occasions for strikes. (*c*) Another important cause has been protests against the policy of retrenchment, and in some cases a protest against the victimisation of particular workers. (*d*) A number of strikes have also occurred on account of other causes like the demand for the grant of certain amenities like the supply of free quarters, or house rent allowance, or the removal of an officer etc.

The State and settlement of strikes : The occurrence of industrial unrest of course affects both the workers or employers. The workers suffer loss in earnings and other privations. The employers have to bear losses in profits. It also affects the community seriously in many ways. Strikes lead to a decline in output, lower national income and so affect everybody. Whenever strikes take place in an industry, the whole atmosphere becomes surcharged with extreme uneasiness and suspicion, and the State is often forced to intervene to prevent breaches of peace. Under the circumstances the government had often to intervene and adopt suitable measures for the prevention and settlement of industrial disputes.

The large-scale occurrence of strikes after 1920 drew the attention of some state governments to the necessity of devising measures for

the settlement of disputes. But no definite legislation resulted until 1929 when the Government of India passed the *Trade Disputes Act.* Under that Act, government obtained the authority to refer a dispute either to a Court of Enquiry or a Board of Conciliation. A Court of Enquiry was to consist of one or more persons who were to report on specific matters referred to them. A Board of Conciliation was to consist of an independent chairman and other members appointed by the government. The function of a Board was to bring the parties together and induce them to come to a settlement. In the absence of a settlement it was to investigate the dispute and report to the government. The Act made a distinction between public utility services such as railways, posts and telegraphs etc., and other industries. In the former no strike could be declared without giving 14 day's notice. No strike could be declared in any industry which had any objective other than the furtherance of a dispute in that industry. In other words, general strikes or strikes for political purposes were prohibited. This Act was originally passed for five years, but was later made permanent. Though a large number of strikes occurred after its passage. its provisions were invoked only in a small number of cases. It remained virtually a dead letter. Later in 1938 the Government of India passed the Trade Disputes Amendment Act under which the State governments were authorised to appoint conciliation officers and the Central Government might also appoint conciliation officers in respect of a railway company.

In the meantime the Bombay Government passed a number of Acts in 1934 and 1938 under which greater emphasis was put on methods of conciliation of disputes. These Acts provided for the appointment of conciliation officers, setting up of Boards of Conciliation, and lastly, of a permanent Industrial Court for the conciliation and settlement of disputes with definite time-limits specified in each case. All disputes must be submitted before these bodies before any strike or lockout could be declared. But the acceptance of awards was not obligatory. The Act of 1938 also provided for the recognition of trade unions by the employers.

The Second World War broke out in 1939, and under rule 81A of the Defence of India Rules, it was provided that the Central Government might prohibit strikes and lockouts in essential industries, and might refer all disputes for conciliation or adjudication. No strike or lockout could be declared during the pendency of conciliation

proceedings. The Central Government might also declare an award to be binding upon both the parties. Thus for the first time this legislation introduced compulsory reference of disputes to adjudication and compulsory adjudication on an all-India scale.

As in the case of the Trade Disputes Act of 1929, the Rule 81A of the DI Rules was not much enforced, though a number of strikes took place during the war period. The end of the war and the advent of independence witnessed the occurrence of many strikes, whose number increased from 820 in 1945 to 1629 in 1946 and 1811 in 1947. The number of workers involved jumped up from 7·47 lakhs in 1945 to 19·61 lakhs in 1946 and 18·40 lakhs in 1947. As a result, the government was forced to intervene. and passed the Industrial Disputes Act in 1947.

Industrial Disputes Act of 1947 : This Act still forms the basis of the machinery for the settlement of disputes. At the bottom there are to be works committees in every factory employing more than 100 workers. These committees are to consist of representatives of the management and of the workers, the latter to be elected by the votes of workers. It will be the business of the works committee to try to settle the day-to-day differences by mutual discussion. Secondly, the Act seeks to set up another machinery for conciliation of disputes. The government would appoint a number of conciliation officers, who would go to the factory or establishment, and try to induce both the parties to come to a settlement. Whether they achieve success or failure, they must report back within 2 weeks to the government. The government may then refer the dispute, if still unsolved, either to a Board of Conciliation or to an Industrial Tribunal. If the industry is declared to be a public utility industry, the dispute must be so referred. A Board of Conciliation is to consist of an equal number of representatives of workers and employers and an independent chairman to be appointed by the government. This Board's function will be to induce both the parties to come to a settlement. Whether successful or not, the Board must report within 2 months to the government.

An industrial tribunal consists of one or more members, who must possess the qualifications of a High Court Judge. The tribunal acts like a court, hears the arguments of both sides and gives an award. The awards of the tribunal are binding on both the parties for one year except in establishments owned by the government.

The Act prohibits all strikes or lockouts during the period of conciliation or arbitration and during the periods for which awards are declared to be binding.

This Act thus provides the machinery for both the conciliation of disputes and for compulsory arbitration. But in subsequent periods recourse had increasingly to be made to the provisions for compulsory arbitration, while Boards of Conciliation were set up only in a few cases. This was a serious defect in the working of this Act. Secondly, it happened that different industrial tribunals gave conflicting judgments on important matters, and this created confusion in the industrial field. So the government had to pass an amending Act in 1950, providing for the setting up of an Appellate Tribunal to hear appeals from the awards of different industrial tribunals, industrial courts, wage boards etc.

For the time being this Act and the famous Industrial Truce Resolution succeeded in arresting the increasing tempo of strikes. The number of strikes declined from 1811 in 1947 to 1259 in 1948 and 814 in 1950, and the number of workers involved came down from 18·41 lakhs to 7·20 lakhs during the same period. There is no doubt that during a period when industrial relations were extremely strained, this act provided the machinery for the settlement of disputes. True, there have been important defects in that machinery. It was unfortunate that gradually the conciliation machinery was put into cold storage while compulsory adjudication came to play the leading role. This was not the fault of the machinery provided by the Act. Conciliation proceedings presuppose the existence of a spirit of compromise among both employers and the workers, and this was absent in the vast majority of cases. Hence the defects in the machinery become prominent. But in justification of the Act one may say that it passes the wit of man to devise a satisfactory machinery for the settlement of industrial disputes.

Labour Relations Bill of 1950 : In view of the criticisms of the Industrial Disputes Act of 1950, the government introduced a new Bill, called the Labour Relations Bill in 1950.

The Bill sought to provide an elaborate machinery for the settlement of disputes. As in addition to the settlement of disputes, it includes certain provisions for certifying trade unions as a bargaining agent, it has been called the Labour Relations Bill. The Bill provided for the establishment of works committees in all establishments with no limit

on the number of workers. The business of these committees was to adopt measures for securing and preserving amity and good relations, for increasing production and for settling disputes. Besides works committees, it retained the usual set-up of conciliation officers and *ad hoc* boards of conciliation as in the 1947 Act. But it sought to introduce a new body, "Standing Conciliation Boards" to be constituted for any area or any class of establishments. These were more or less to be permanent bodies entrusted with the task of conciliation of disputes. Such a Board would do away with the delay involved in setting up of an *ad hoc* board in each dispute.

Another innovation under the Bill was the establishment of a number of Labour Courts, consisting of a person who had been or was a member of the judicial and executive service. A Labour Court was to have two sets of functions, *viz.*, to hear both sides in a dispute and pronounce its judgment which was to be binding upon both the parties and secondly, to consider applications made by trade unions for certification as bargaining agents.

In addition, there would be labour tribunals, *ad hoc* bodies as at present, and an Appellate Tribunal constituted by the central government to hear appeals against any award of a tribunal, and to exercise superintendence over all Labour Courts and tribunals.

The Bill came in for a good deal of criticism, and was allowed to lapse with the dissolution of the Parliament. From time to time it is reported that the government is contemplating the introduction of a new Bill on this subject.

Changes in the Industrial Disputes Act : Important changes in the machinery for the settlement of industrial disputes have been introduced in the new Industrial Disputes Act of 1957. This Act proposes to set up three types of tribunals for the settlement of an industrial dispute :—labour courts, industrial tribunals, and national tribunals. The Labour Court will have jurisdiction to adjudicate on industrial disputes relating to such matters as the legality or propriety of an order passed by an employer under the standing orders, the discharge or dismissal of employees and illegality or otherwise of a strike or lockout. An industrial tribunal will adjudicate on disputes relating to wages, hours of work, bonus, rationalisation and retrenchment. A national tribunal will adjudicate on matters involving questions of national importance or on disputes affecting establishments situated

in more than one State. The Act abolishes the Appellate Tribunal. The Act also enlarges the definition of a "workman" so as to cover technical staff and supervisory personnel whose emoluments do not exceed Rs. 500 per month. It also lays down that the employer shall not introduce any change in respect of certain specified matters affecting conditions of work without giving at least 21 days' notice to the workers. It also amends the Industrial Employment (Standing Orders) Act so as to empower both the certifying officer and the other authorities concerned to take into account the fairness or reasonableness of the standing orders before they are certified. Further, a worker is empowered to apply to the certifying officer for modification of the standing orders as also to refer the question of the application or interpretation of a standing order to the Labour Court. One important concession given to the employer is the provision that he may, during the pendency of a dispute, discharge or punish an employee for any misconduct not connected with the dispute.

The new Act has not done much to incorporate the so-called "Giri" approach in labour relations. Only one important clause, providing for arbitration, may be said to bear the impact of this approach. It lays down that it is open to both the parties to sign an arbitration agreement and refer the dispute to an arbitrator. Excepting for this feature, the new Act follows, more or less, the beaten track, being modelled rather closely on the Bombay Industrial Relations Act. The abolition of the Appellate Tribunal is a step in the right direction as its presence was encouraging a rather impossible litigious psychology among both the parties to a dispute. The absence of this body may possibly induce a sense of realism among both employers and employees.

Compulsory Adjudication *vs.* Conciliation : The Industrial Disputes Act of 1947 included a machinery both for the voluntary conciliation of dispute and for compulsory adjudication. In the application of the Act, the first method was comparatively neglected, while recourse was increasingly had to the second. The working of the machinery of compulsory adjudication by which industrial tribunals decided disputes and gave awards which were binding upon both the parties, gave rise to certain difficulties, and there was a reaction against this method. Mr. Giri, who became the Central Minister for Labour during this period, became convinced of the inadequacies of compulsory adjudication, and in his address at the 12th session of the Indian Labour

Conference in October 1952 pleaded for less reliance on compulsory adjudication and for more emphasis on the voluntary conciliation of disputes. This is the famous "Giri **approach**," according to which attempts are increasingly to be made to settle all industrial disputes by mutual negotiations between both the parties, failing which conciliation officers are to be approached. If the efforts of the officers also fail, the parties should agree voluntarily to refer the dispute to arbitration. The award of the arbitrators is to be binding upon both the parties. If arbitration fails, the matter should go before an umpire to be chosen by both sides. In general, emphasis is to be put on the methods of voluntary conciliation and arbitration and reference to compulsory adjudication is to be made only in cases of emergency and in public utility services.

As a general rule, the validity of the Giri approach, *i.e.*, voluntary conciliation and arbitration of disputes, is beyond doubt. An industrial dispute is not like an ordinary lawsuit, a matter of the correct interpretation of the law and existing rights. Any solution in such a dispute must be a compromise based on the claims of both the parties. Such a compromise solution is likely to be cheerfully accepted and worked if it has been arrived at by the mutual agreement of the parties themselves. If the compromise is imposed by an outside authority, as in the case of an award by industrial tribunals, neither party may feel any loyalty to carry out its terms conscientiously. There are many indirect methods of stultifying an award one does not like without declaring a formal strike. Labour may, for example, adopt go-slow tactics, while employers may impose great delays in carrying out the award on various pretexts. So even if formal peace is maintained, labour-capital relationship remains extremely unsatisfactory, and the seeds of future disputes remain in the industrial field.

Secondly, industrial tribunals all consisted of judges or men possessing high judicial qualifications. These persons, however independent or neutral they may be, are not always the best men to decide industrial disputes. The determination of such disputes necessitates a thorough knowledge of the technical conditions prevailing in each industry, and these judges do not always possess such knowledge.

Thirdly, compulsory adjudication may prevent the growth of habits of collective bargaining. When workers know that they can always

go to an outside body (*i.e.* a tribunal) for a decision on the dispute, they may not be so willing to come to an agreement with the employers. They may not even feel the urge to join a trade union as recourse to the tribunal will give them what they may not be able to secure through a trade union.

Lastly, the system of compulsory adjudication has not actually brought about industrial peace in the country. On the other hand, it encouraged disputes and tended to magnify the difference between employers and workers. Moreover, different tribunals have given conflicting judgments on the same matter. and this has complicated the working of the industrial machine.

The defects of the system of compulsory adjudication of industrial disputes are no doubt well-known. But the substitute proposed by Mr. Giri, *i.e.*, the method of voluntary conciliation and arbitration, pre-supposes the existence of three conditions for its success. First, there should be strong and well-organised trade unions pursuing a constructive policy of improving working conditions in the industry. Secondly, employers should be willing to recognise the unions and be prepared to carry on negotiations with them on equal terms. Lastly, both the unions and the employers should evolve appropriate machinery for the settlement of disputes on which they cannot agree. None of these conditions are present in this country. In the majority of industries, strong and well-organised unions are the exception rather than the rule, while most of the employers have shown an extreme unwillingness to conduct negotiations with the unions. Under these circumstances, collective bargaining habits cannot be developed, and the method of voluntary conciliation cannot be worked successfully.

There is no doubt that the working of the system of compulsory adjudication has been attended with many difficulties. But when everything has been said, one must have to admit the achievements of the system in the background of the fast deteriorating industrial relations in the immediate post-war years. The conditions which prevailed in the industrial field in 1946 and 1947 brooked no delay. They needed a quick-action remedy, whereas the method of voluntary conciliation cannot be applied within a short period of time. The system of adjudication by industrial tribunals has arrested further deterioration of the industrial situation, has introduced rates of minimum wages which are after all not very unreasonable, and has at least helped in

bringing about industrial truce, if not peace. Adjudication of industrial disputes by judges may not provide a perfect method. But it means the review of the dispute by independent critical minds, and by people trained to decide disputed points, and as such, these awards are likely to provide the best available compromise, especially when the parties have failed to come to an agreement.

The Giri approach may be sound in theory, and desirable in practice. But it is doubtful how far it can be carried out in actual practice in view of the state of development reached by trade unions in our country. Now that the post-war crisis in industrial relations has successfully been overcome, time has arrived for a recourse to the slow-moving but permanent method of voluntary conciliation. Emphasis should now shift from compulsory adjudication to voluntary conciliation in the settlement of all disputes. But the former method should be kept in the reserve, ready for action, and should at once be thrown into the battle, whenever or wherever voluntary conciliation fails to yield results.

Questions

1. Trace the growth of the trade union movement in India. Describe the present position of the trade unions (C. U. 1961)

2. What are the strength and weakness of the labour movement in India ?

"The obstacles to the development of trade unions in this country are largely internal ; they come from labour itself." Elucidate. (C. U. 1961 ; B. Com. 1957).

3 What are the causes of industrial disputes in India ? Describe the steps taken by the government to settle industrial disputes. (C. U. B. Com. 1960)

4. Discuss the causes of labour unrest in India in recent times. What measures have been adopted by the Government of India for the promotion of industrial peace ?

5. Briefly describe the existing machinery for the prevention and settlement of industrial disputes. What modifications would you suggest ?

6. What methods have been devised to bring about Labour-Management Co-operation since the outbreak of the Second World War ?

7. Examine the scope of compulsory adjudication in the settlement of industrial disputes in India.

8. Write notes on the Giri approach forwards compulsory adjudication.

CHAPTER 29 LABOUR LEGISLATION AND WELFARE

In addition to the labour laws we have already reviewed, the government has also passed a number of other laws for improving the conditions of labour. These are the various Factory Acts, the Mining Labour Acts, the Plantation Labour Acts, Payment of Wages Act, Workmen's Compensation Acts and Maternity Benefit Acts. For the sake of convenience, we propose to study these Acts in three periods,—the period before the World War I, the period between two world wars, and the Post-World War II period.

First period—upto 1914 : The first labour legislation in India was passed in 1863 and it sought to regulate the system of recruitment of labour in the tea gardens. It laid down that all recruiters were to be licensed and all emigrants were first to be registered before the District Magistrate before they were sent to the gardens. This was followed by other Acts in 1865, 1870 and 1873, all dealing with labour in tea gardens.

The next important piece of legislation is the *Factory Act of 1881*, the first Factory Act. It prohibited the employment of children under 7 years of age and those between 7 and 12 years were not to work for more than 9 hours a day with an hour's daily rest and 4 holidays per month. But this remained a dead letter on account of difficulties of enforcement. At the end of 10 years, the *Second Factory Act* was passed. It raised the minimum age of children from 7 to 8. Hours of work of children between 9 and 14 years were to be restricted to 7 hours a day. Women workers were to work only between 5 A.M. and 8 P.M. and for not more than 11 hours a day with one and a half hours' daily rest. Men were to be given half hour's daily rest and one holiday every week.

This Act remained in force for 20 years. In the meantime a Committee in 1906 and a Commission in 1907 were set up to enquire into the working conditions in the factories. Following their recommendation, the *Third Factory Act* was passed in 1911. It reduced the hours of work for children to 6 and to prevent evasion, it was laid down that the age and physical fitness of children were to be certified by qualified medical practioners. For the first time the hours of work

of adult workers were limited to 12 hours a day with daily rest of half an hour. In 1901 the first Indian Mines Act was passed. It was a minor legislation.

Second period (1919-1939): The second period saw the passage of many labour laws. The provisions of the Factory Act of 1911 were felt inadequate, and the *fourth Factory Act* was passed in 1922. It raised the minimum age of children to 12. Those between the years 12 and 15 were not to work for more than 6 hours a day with a half-hour interval after 4 hours of work. In the case of adult male workers, hours of work were fixed at 11 a day with one hour's daily rest, and a maximum of 60 hours a week. The employment of children and women in certain dangerous processes was prohibited.

The next important Factory Act came in 1934 as a result of the recommendations of the Royal Commission on Labour. This Act reduced the hours of work of children to 5 hours a day. The hours of work of adults were reduced to 10 per day with a maximum of 54 hours a week. Factories supplying daily necessities could, however, work 56 hours a week, while seasonal factories work 60 hours a week and 11 hours a day. Factories must provide drinking water, first-aid boxes, and cretches where 50 or more women were employed etc. This Act was further amended in 1936 giving wider powers to the State governments to bring workshops not using power within the operation of the Act.

While Factory Acts were passed to govern working conditions in all factories, special legislation was necessary to deal with the conditions prevailing in other industries. Thus the Indian Mines Act was passed to carry out the recommendations of the Washington Conference. This was applicable to coal mines where the employment of children under 13 years was prohibited. It authorised the State governments to prohibit the employment of women underground. The hours of work of adult labour were fixed at 60 hours per week above ground and 54 hours underground. A subsequent amendment in 1928 fixed 12 hours as the maximum working period per day.

The Indian Mines Act was further amended in 1935. It reduced the hours of work to 10 per day with a maximum of 54 hours per week above ground. For underground work the daily limit was fixed at 9 hours. No children under 15 years can be employed in or about a mine. Women cannot be employed underground.

With regard to plantations, the most important legislation during this period was the Tea Districts Emigrant Labour Act of 1932. It provided for the appointment of a Controller of Emigrant Labour in Assam whose duty would be to look after the interests of tea garden workers. Recruitment of such workers was to be made only by approved persons who were licensed. The workers were given the right to be repatriated at the expense of the garden at the end of 3 years' service, or earlier in cases of ill-health.

This period also saw the passage of beneficial labour legislation in many directions. The *Payment of Wages Act of 1936* was passed to deal with the abuses existing with regard to the methods of wage payment. It fixed the maximum wage period at one month and wages must be paid within 7 days from the date of expiry of the month in establishments employing less than 1000 persons and within 10 days in bigger establishments. It laid down the grounds on which deductions could be made from wages and fines imposed on workers could not exceed half an anna in the rupee and the amount so realised must be spent on purposes beneficial to workers.

Workmen's Compensation Acts, seeking to fix rates of compensation to be paid by employers to workers who have suffered an injury in course of their employment, were passed in 1923, 1926, 1929, 1931 and 1933. These Acts fixed the amounts to be paid to workers in cases of temporary disablement, permanent disablement and death, the amounts varying with the average wage rates. Those who received a wage of less than Rs. 10 per month were to be paid Rs. 500 in case of death, Rs. 700 for permanent disablement and a month and a half's wage for temporary disablement. A Commissioner for Workmen's Compensation has been appointed and a worker or his dependents in case of death could appeal to him if the employer refused to pay the compensation. Maternity Benefit Acts were passed in several States during this period. These Acts seek to ensure the payment of a cash sum to women workers a few weeks before and after child-birth.

Third period (1945—): The post-war years have witnessed a spate of labour legislation, among which we have already discussed the provisions of the Industrial Disputes Act of 1947, the Minimum Wages Act of 1948, the Employees' State Insurance Act of 1948, and the Employees' Provident Fund Act of 1952. In addition to these the government has passed the Industrial Employment Act of 1946, the

Factory Act of 1948, Mines Acts of 1949, and 1952, the Plantations Labour Act of 1951 etc.

With regard to factories, an amendment passed in 1946 had already reduced daily hours of work to 8 per day and the weekly maximum to 48 hours for perennial and 54 hours for seasonal factories. A comprehensive *Factory Act* was later passed in 1948. It prohibited the employment of children below 14 years and those between 14 and 15 have to be treated as children. The hours of work for children were to be reduced to 4½ per day. For adults hours of work were fixed at 48 hours in a week. They were to be granted at least half an hour's rest after 5 hours of work. Besides weekly holidays, every worker must be given leave on full pay after a year's service at the rate of one day for every 20 days of work. The daily and quarterly limits of overtime have also been fixed and overtime work has to be paid at twice the normal rates of wages.

This Act has also provided for the appointment of Welfare Officers in factories employing 500 or more workers. A canteen is also compulsory in factories employing 250 or more workers. Provisions have been made for the compulsory licensing and registration of new factories, and for securing the health, safety and welfare of the workers. The Act has been made applicable to all factories using power and employing 10 or more workers and to those not using power but employing 20 or more workers.

The Industrial Employment Act of 1946 requires every owner of a factory employing 100 or more workers to submit copies of Standing Orders containing particulars of workers employed and the conditions of work.

The Mines Act of 1949 fixed working hours in coal-mines to 48 hours per week with 9 hours per day for work above ground and 8 hours a day for work underground. It has fixed the rates of overtime work at 1½ times the ordinary rate for work above ground and twice the ordinary rate for work underground. Subsequently another Act was passed in 1952, consolidating all existing laws relating to the employment and conditions of work in coal mines. The government has also passed the Coal Mines Labour Welfare Fund Act which levied a cess on coal to be utilised for constructing houses and providing other amenities for workers in coal-mines. A Coal Mines Provident Fund Act has also been passed, establishing provident funds for workers who

contribute at the rate of one anna in the rupee on their basic pay, the employer contributing an equal amount.

The Plantations Labour Act of 1951 seeks to incorporate with suitable modification the main provisions of the Factory Act to the case of tea gardens. It provides for such amenities as the supply of drinking water, canteens and cretches, medical and educational facilities, hours of work and weekly holidays etc.

Labour welfare: The term, labour welfare, includes such provisions as facilities for rest and recreation, canteens, sanitary and medical facilities, transport arrangements and housing of workers. These facilities are meant to enable them to work in healthy, and congenial surroundings and are expected to improve their morale, health and working life.

The Central and State governments and many of the enlightened employers have adopted a number of measures to promote labour welfare. The Bombay Government, for example, have opened about 50 welfare centres where there are facilities for indoor and outdoor games, sports, gymnasium, playgrounds for children, entertainments for cinema shows etc. Under the Factory Act, employers have a statutory obligation to make provisions for canteens, cretches, drinking water etc. Labour welfare funds have been set up by legislation in coal mines, mica mines etc.

The Government of India is considering proposals for enacting a Labour Welfare Fund Act for the purpose of setting up labour welfare funds on a statutory basis. At present the State governments are attempting to induce employers to set up such funds on a voluntary basis. But not much progress has been achieved on this point owing to the fear of the employers that this would impose fresh burdens on industries. It is proposed that all fines collected from employees under the Payment of Wages Act, and Minimum Wages Act, all unpaid accumulations in the shape of unpaid wages, bonus or gratuities and any other voluntary donations should be taken to constitute these funds whose management would be entrusted to Boards composed of equal numbers of representatives of workers and employers, plus any other members nominated by the government. It should be noted that Bombay has already passed such an Act under which employers are compelled to contribute to the Fund.

Profit-sharing : The idea behind the introduction of schemes of profit-sharing is to raise productivity of the industry through better industrial relations. The workers are to be given, in addition to their wages, a part of the net profits of the concern in accordance with a mutually agreed formula. This would raise workers' incomes, improve their efficiency and willingness to work, as they would also share in the extra profits that the firm would earn as a consequence. Such schemes have been introduced in the western countries.

The question of the introduction of profit-sharing in Indian industries was taken up for consideration in 1948, when the Government of India set up a Committee to examine the different schemes. The Committee on Profit-sharing, as it was called, recommended the adoption of profit-sharing as an experimental measure, for a period of 5 years in six major industries like cotton textile, jute, steel, cement, etc. According to its recommendations, the net profits of a concern, after deducting 6 p.c. return on paid-up capital and reserves, should be distributed on a 50 : 50 basis between the shareholders and the workers. Any individual workers' share in these profits was to be determined on the basis of his earnings during the previous 12 months. He would be allowed to take his share in cash up to a maximum of 25 p.c., the rest to be credited to his provident fund or to any other fund.

The schemes have not been put into effect except in one or two concerns on a purely voluntary basis. There are large difficulties with respect to all schemes of profit-sharing. If workers are to be given a share in profits, should they also agree to shoulder the burden of losses with their employers ? Profits do not always depend on the work or efficiency of the workers. Workers may have worked harder in the expectation of getting a share of the increase in profits. But an adverse turn of the market may convert profits into losses. It would then cause much disappointment among workers who may not always understand the intricacies of the market, and in their frustration, they may feel great bitterness against their employers.

While profit-sharing has not made much progress in Indian industries, a number of industrial concerns have adopted schemes for bonus-sharing with their employees. In such schemes, the employees are granted annual bonuses, determined according to a pre-arranged formula or on an *ad hoc* basis. In some agreements, the amount of the bonus to be paid to the workers is linked in some way to the profits of the concern, while in others, there is no such link. According to some

authorities, the present system of payment of bonus to the workers is nothing but a method for paying deferred wages. Recently the Government of India has set up a Bonus Commission to examine all such schemes of bonus sharing and to recommend suitable modifications in these schemes to change them into profit-sharing. The report of the Commission was published in 1964. and the government passed the payment of Bonus Act in 1965. The Bonus Commission recommended that 60 p.c. of the available surplus, *i.e.*, gross profits of a concern minus its depreciation, income tax and profits tax, dividend on preference shares, dividend on ordinary shares at 7 p.c., and return of 4 p.c. on reserves, should be distributed among the workers as bonus, subject to a maximum of 20 p.c. of the annual basic wage and DA or a minimum of Rs. 40, whichever was higher. The minimum bonus is to be paid whether the concern earns profit or not, and the maximum is not to be exceeded even if the concern earns very large profits. If the concern does not earn profits for paying the minimum bonus, it can carry the loss forward to subsequent years and set on against its future profits. The Act passed by the government retains these provisions regarding the payment of the minimum and the maximum bonus. But the rates of return to be deducted from gross profits have been raised. Thus 8·5 p.c. dividend on ordinary shares and 6 p.c. on reserves are to be deducted from gross profits before the payment of bonus.

Questions

1. What steps have been taken for the protection and improvement of industrial labour in India ?

2. Give a brief account of the chief legislative measures adopted to promote the welfare of industrial labour in India.

3. Describe the landmarks in the history of factory legislation in India during the past 40 years. Discuss their influence on the efficiency of labour.

CHAPTER 30 TRANSPORT

The economic development of a country is bound up with its system of transport. The different means of transport,—railways, cars, aeroplanes and shipping—carry goods and men and thus help in spreading knowledge, culture and civilisation. No country can advance industrially unless it develops its means of transport to an adequate extent. In fact, statistics regarding transport may provide a good index of the state of development or under-development of a country.

There are in general four kinds of means of transport,—railways. roads, shipping and aeroplanes. We propose to study them one by one.

Railways : The beginnings of railway construction may be traced to the year 1844 when the East India Company sanctioned the construction of the E. I. Ry. and the G. I. P. Ry. The late Lord Dalhousie in a famous Minute laid down the routes to be followed by the railways. In accordance with his plans contracts were made with the British railway companies for the construction and management of railways in India subject to certain guarantees. The chief guarantee related to the payment of at least a minimum dividend of 5 p.c. on all capital supplied by the companies at fixed rates of interest. As the railways were constructed under a guarantee, the system came to be known as the *old guarantee system.* The railways failed to earn the 5 p.c. dividend, and the deficit had to be made up by the government according to the guarantee. So from 1869, for about 10 years, the government itself constructed a number of railways out of its own funds. As State management was then against the prevailing political philosophy. these and other railways acquired by the government were handed back from 1879 to British Companies under a new guarantee system, when the minimum guarantee rate of dividend was lowered to 3½ p.c. With the end of the 19th century, railways began to earn good profits and the government was no longer called upon to finance the deficit.

The end of the first world war led in 1930 to the appointment of the Acworth Committee which advocated the system of State management of railways and pleaded for the separation of railway finance from the control of the general budgetary system. These proposals were accepted by the government and one by one almost all the railways have been acquired by the State which is also managing the railway system of the country. The Indian taxpayer is now the full owner of the railways.

Present position. For a single industry, railways employ the largest amount of capital in this country. Total capital invested in railways amounted in 1961-62 to Rs. 1690 crores, compared to Rs. 628 crores invested in joint-stock companies in India. Railways employ more than eleven lakh workers, the largest employer of labour in the country. In 1961-62, the total railway mileage amounted to 57,089 km. The Indian railway system is the largest in Asia and the second largest in the world. But in spite of this development India is very backward as compared to other countries. India has only 9·4 miles of railways per one lakh population, as compared to 465 miles in Canada, 224 miles in the U.S.A. and 46 miles in the U.K. There is still a great leeway to be made up in railway construction before this country can claim to be properly developed.

Organisation of railways : Originally the administration of railways was in charge of a Department. Later in 1905, a separate Railway Board with a Chairman and two members was appointed to administer the railways. Changes were made in the membership of the Board from time to time.

Zoning system. Below the Railway Board, the administration has been divided into eight zones. The zones have been fixed in such a way that each unit has a compact region consisting of about 5,000 miles of railway. It has been claimed that the zones are large enough to support a headquarter's organisation, capable of adopting the most recent improvements in railway technique and to be equipped with proper workshop facilities and research institutions. The zoning system is supposed to be an improvement upon the previous chaotic system of railway organisation.

Railway finance : Till the end of the 19th century the working of railways involved the government in considerable losses. In order to attract British capital for railway construction the government gave a guarantee regarding the payment of a minimum dividend, first at 5 p.c. and subsequently at 3½ p.c. on all capital invested. As the railway companies failed to earn this amount, the government had to meet the deficit. The total amount paid by the government during these years amounted to Rs. 58 crores.

After 1898, the Railways began to earn surpluses, and this has continued, with occasional breaks, up to the present day. Before 1924 railway finance was a part of the general budget of the Government of

India, and was subject to all the budgetary rules. Unlike other government departments, railways are a commercial proposition, and so the rules which were considered appropriate for other government departments actually hampered the working of railways. For example, the other departments were subject to the doctrine of the lapse, according to which, if any department failed to spend the budgetted amount within 31st March of each year, the unspent balance would be merged in the general budget. This may be allright for other departments. But the application of this rule to railways led to considerable extravagance as each branch hastened to spend every pie before the sunset of 31st March. Moreover, every commercial concern must make adequate provisions for depreciation and keep a considerable reserve fund. But in the absence of proper commercial accounting, little provision was made for depreciation, and the reserves of the railways were negligible.

For these reasons the Acworth Committee recommended the separation of railway finance from the general revenues of the government. This was accepted by the latter, and in 1924, a formal resolution to that effect was approved by the legislature. Arrangements were made for framing a separate budget for railways, subject to the condition that the railways were to make some contributions to the general revenues. The rate at which such contributions were to be made was laid down in that Resolution.

According to the Resolution, the railways were to contribute to the general revenues at the following rates :—one per cent of the capital at charge at the end of each year plus one-fifth of the surplus profits in that year after deducting the interest on capital at charge of strategic lines and the loss in their working. If, after the payment of such contribution, the amount available for transfer to the reserve exceeded Rs. 3 crores, one-third of the excess should be paid to the general revenues. After making all these payments, the remaining profits were to be carried over to the Railway Reserve Fund, which was to be used, first, to secure the payment of the annual contribution to the general revenues, if necessary, and for arrears of depreciation and for other purposes.

This convention was adopted in 1924, and from that year upto 1930-31 the railways were able to contribute a total of Rs. 41·65 crores to the general revenues. But from that year the railways failed to earn sufficient sums to meet the contributions. This was due to the effects of

the world trade depression. At first the Reserve Fund was exhausted and later loans were taken from the Depreciation Fund to meet the contributions. Afterwards contributions had to be suspended as railway earnings dwindled to very low figures. But the earnings improved from 1937-38 and during the Second World War, these improved to such an extent that the railways were able to pay off the whole of the suspended contributions by the end of 1942-43. By 1945-46, railways were able to contribute Rs. 158 crores to the general revenues.

The convention of 1924 laid down that it should be reviewed periodically. Following the recommendations of the Kunzru Commission of 1949, this convention was reviewed by the government, and a new convention was adopted from 1950-51. It was laid down in the new convention that the railways should contribute 4 per cent per year on all capital invested in them to the general revenues. A minimum contribution of Rs. 15 crores should be made to the Depreciation Reserve Fund, and a Railway Development Fund should be constituted for the purpose of providing more amenities for passengers, for labour welfare, and for the construction of new lines which might prove unremunerative. The revised Financial Convention of 1955-56 provided for the same rates of contribution except that on new lines a moratorium was to be granted during construction and for 5 years to follow. The Railway Convention Committee of 1960 recommended a dividend of 4½ p.c. during 1961-66. The budget of 1962-63 provided for a dividend of 5 p.c.

The payment of a dividend at 5 per cent to the general revenues makes the taxpayer a shareholder in the railways entitled to a fixed rate of dividend. The railways benefit as they would be able to build up proper reserves and to carry out a comprehensive programme of rehabilitation and expansion.

Railway rates : The Indian railways were originally managed by British Companies which were free to fix rates of freight, subject to the maximum and minimum rates fixed by the government. In the early stages these companies were interested mostly in the development of foreign trade. So they adopted a freight policy designed to encourage the flow of traffic to and from the main ports. As Indian industries came to be developed, they had to face some difficulties on account of this characteristic of the rate structure. For example, the rates charged for carrying imported sugar from the ports to inland centres

were less than the rates charged on the transport of sugar between two inland centres, even though the distance travelled in the second case was smaller than that in the first instance. Moreover, the fixation of railway rates on this basis has led to the congestion of industries in the port towns. The industrialists have naturally set up their factories in or near the ports in order to take advantage of the comparatively low freight rates from and to the ports. As a result, the location of industries has become uneven and lop-sided.

There was another way in which the fixation of railway rates hampered the development of industries. There were different railway companies, and each railway charged rates only for the length that the traffic moved on its own system, irrespective of the total mileage which the traffic was to travel. When goods travelled on two lines, the rates were not charged on the basis of the total distance, but on the distance travelled over each line separately. As a result, these rates proved to be prejudicial to the smooth growth and even distribution of Indian industries.

In view of these complaints the Acworth Committee recommended the establishment of a Railway Rates Tribunal. The government, however, set up a Railway Rates Committee to consider all complaints against the fixation of rates. The committee had limited powers. But it was able to remedy some of the glaring defects in the rate structure. Later in 1949, the Government of India have established a Railway Rates Tribunal, consisting of a President and two members, who were judges of High Courts. The Tribunal is to examine all complaints regarding unreasonable rates, and its decision is binding upon the railways.

Roads : Roads provide the most ancient means of transport. The Kings and Emperors in ancient India were, like the Romans, fond of building roads all over the country. Sher Shah is credited with building the great trunk roads to facilitate the movement of the army to different parts of the country. The British also constructed a number of important roads. At the present moment it has been estimated that India possesses total roads covering 3·94 lakh miles, of which about 144 thousand miles of roads are metalled and the rest are unmetalled. Compared to the area of the country, this is clearly inadequate. The relative backwardness of India's road mileage will become evident when it is remembered that the average road mileage per lakh of population

is 69·1 in India as against 449·0 in Belgium, 1221·00 in France and 2143·7 in the U.S.A. The average road mileage per square mile of area is 0·2 in India, 2·0 in the U.K. and 2·4 in France. Moreover, of the existing roads of India, a large percentage is ill-kept, and about 1·44 lakh miles are motorable, while the mileage of unsurfaced roads is 2·50 lakhs in 1960-61. This is clearly inadequate. While railways transport has its utility, roads link the villages with the railways and important marketing centres. They, therefore, provide the first link in the distribution of agricultural commodities. Without a good system of roads, perishable goods would run to waste and land would be fallow. Besides bringing important benefits to agriculture and industry, good roads serve the people in another way. They help in bringing the villager to schools and to contact with urban life, and thus quicken the pace of the mental development of these people. Roads have thus an important cultural aspect.

Realising the need for building more roads, the Government of India appointed a Road Development Committee in 1927 to examine the question of road development. The Committee suggested that the Central Government should build and maintain the Great Trunk Roads, while the State governments and local bodies should look after other roads. They also recommended the levy of an additional duty of 2 as. per gallon on petrol, the proceeds of which were to be credited to a separate fund, known as the Road Fund. Grants should be made from this Fund to the State Governments for the construction of roads. The government accepted these proposals and constituted the Road Fund, which was put on a permanent basis in 1934.

In 1943 the Government of India convened a conference of Chief Engineers at Nagpur to consider the ways and means of road development. The conference drew up a 10-years plan for road development, which came to be known as the Nagpur Plan. According to this Plan, roads were classified at National Highways, State Highways, District Roads and Village Roads.

The *National Highways* would follow the existing trunk roads and would connect the capitals of states, ports and large towns. This construction and maintenance would be the responsibility of the Central Government. At present there are about 13,400 miles of these roads, of which the more important are the Grand Trunk Road, Calcutta-Madras Road etc.

State Highways are to be maintained by the State Government. They would connect the district headquarters and important towns within the State with the National Highways.

District roads and village roads are meant to connect the villages and other important areas within the district with the highways and railways. They are to be built and maintained by the local bodies. Most of these roads are unmetalled and unmotorable during the rains.

The general idea behind the plan was that roads should be built in such a way that no village would be more than 5 miles from a main road. Owing, however, to certain difficulties regarding finance and materials, this Plan had to be cut down to a considerable extent. The Government of India had set up a Road Board and a Central Road Research Institute.

Roads in the Third Five Year Plans : The expenditure on the development of roads was about Rs. 155 crores in the First Plan, and was about Rs. 250 crores during the Second Plan. It is expected that during these two plan periods, the mileage of all surfaced roads other than municipal roads would increase from 98,000 in 1950-51 to 1,44,000 in 1960-61, *i.e.*, by about 50 p.c. In the Third Plan the total amount allotted for road development is Rs. 250 crores and on the basis of this expenditure it would be possible to construct another 20,000 miles of surfaced roads in the next 5 years.

Motor transport : Bullock carts and motor vehicles use the roads to carry passengers and goods. The former is the most ancient means of transport, and at the present moment it has been estimated that India possesses about 87 million bullock carts, providing employment for about one crore of people and carrying over a hundred million tons of goods and a large number of passengers. Bullock carts still play a very important role both in the rural and urban areas.

Motor vehicles provide the best means of road transport. Their great merit is flexibility. They can easily collect and distribute loads and passengers from door to door, and they do not need large capital. But unfortunately the number of motor vehicles is very small, as compared to the size or population of the country. While the U.S.A. has one motor vehicle for every three persons and the U.K. for every 15 persons, India had only one vehicle for every 1350 persons. In 1960-61 the total number of motor vehicles used in India was more than 5,50,000.

Nationalisation of motor transport: In recent years the State Governments have adopted the policy of nationalising road transport. The scheme was started first in Bombay in 1946 when the Bombay Government took over some transport companies. That State has established a State Transport Corporation which owns and operates the transport services. Other States have followed suit, and U.P., Punjab, Himachalpradesh and Bihar have also nationalised some routes and been running a number of bus services. The Governments of Madras, West Bengal and others have started city bus services.

Roads vs. Rails: The growth in motor transport during the twenties of this century gave rise to the problem of serious competition between railways and motor vehicles. As the Wedgewood Committee found that for nearly one-half of the total mileage of railways metalled roads runs parallel to and within 10 miles of railways. As a result, railways have lost a considerable volume of short distance passenger and goods traffic to the motor transport. The latter has taken away the more paying traffic from the railways by quoting lower freight and fares, leaving to the railways heavy traffic which paid a comparatively lower freight.

There are important reasons why motor transport gained at the expense of railways. In the first place, motor transport provides quicker service than railways, especially for short distances. Secondly, motor transport is more flexible than railways. It picks up and delivers goods with greater ease and convenience. It can easily change its routes as conditions require. Owners of goods can also travel on lorries, and can thus keep watch over their goods, preventing theft, whereas the routine on railways is more rigid, and petty thefts are very common. One important argument that is often made against motor transport is that it has not to pay for the roads it uses, whereas the railways have to bear the heavy cost of construction of rail-roads. This is not fully correct as motor transport is heavily taxed by the government in various ways, and the proceeds of the tax on petrol. paid mostly by motor transport, are utilised for the construction and maintenance of roads.

The question of road-rail competition was examined by two Committees—the Mitchel-Kirkness Committee of 1932. and the Wedgewood Railway Enquiry Committee of 1937. The Second Committee recommended that it was only fair that motor transport should be properly controlled, and that joint road-rail companies should be formed to

operate motor transport so that railways could participate in road traffic. In accordance with the recommendations of this Committee, the Government of India passed the Motor Vehicles Act in 1939 which included many provisions for licensing and controlling motor transport. Under this Act motor vehicles were required to operate only under permit, which laid down the maximum number of passengers they could carry, their working hours and conditions etc.

Mere control over motor transport cannot solve the problem. We must recognise that both railways and motor transport have an important part to play in providing a cheap and efficient system of transport. A real solution would lie in dividing traffic between these two methods in such a way that the public received the best service. Motor transport is suited for short-distance or quick traffic. It provides the only means of linking up villages with market towns and other trading centres. The railways are admirably suited for the transport of heavy and long-distance traffic. In this way each will have a separate field of operation and each will act as a complement to the other instead of competing between themselves.

With the gradual nationalisation of road transport, a policy which is being increasingly adopted by the State Governments—the problem has become easier of solution. The different State Transport Corporations or similar bodies have adopted the policy of co-ordinating road-rail transport, thereby avoiding mutually destructive competition.

Shipping : India was once famous for her shipping. She had a flourishing ship-building industry, and her ships sailed to the different parts of the world. But the opposition of the British interests and the introduction of iron-built ships led to decline of this industry in our country.

On the eve of independence in 1947, India had a very small mercantile marine. She had only 1½ lakh tons of shipping which was less than one per cent of the total world shipping. She had no ship-building yards. Though a few Indian shipping companies were started, they had to face serious competition from old-established British rivals.

The necessity for an Indian mercantile marine in a country like India is obvious. India has a long coast line for the protection of which she must have a navy. No good navy can be built up without a mercantile marine, which serves as a naval auxiliary. Moreover, the

development of a mercantile marine is necessary if we are to reduce our dependence on foreign shipping for the transport of essential exports and imports. A mercantile marine will provide new avenues of employment for the youngmen of this country, and will enable us to retain a large share of the invisible income from shipping, which is now taken away by foreigners.

Since 1947 the Government of India is paying increasing attention to the development of a mercantile marine. Coastal shipping has been reserved for Indian companies, and in 1954, 99 per cent of coastal trade was carried on in Indian-owned shipping. The ship-building yard at Visakhapatnam has been taken over by the Government of India, and it has started constructing a number of ships. A Marine Engineering College has been started at Calcutta, besides the Training Ship, Dufferin, and the Nautical and Engineering College at Bombay, for the training of officers for the merchant navy. Indian companies have started regular services to the U.K., Europe and North America. The Government has also taken steps to develop other ports. As a result of these measures, gross tonnage of Indian shipping has increased from 1·5 m. tons in 1939 to 4·35 m. tons in 1953 and to 9·01 lakh tons in 1961. The First Five Year Plan set the target for gross tonnage at 6·0 m. tons in 1955-56. To achieve this tonnage the government advanced loans at low rates of interest to the shipping companies for the purchase of ships. It was also proposed to set up 3 shipping corporations for the development of shipping in overseas trade, of which one has already been started.

During the first two plan periods a substantial addition to the shipping of the country took place. The total tonnage increased from 3·91 lakh GRT in 1950-51 to 6·00 lakh GRT in 1956-57 and reached 9·01 lakh GRT at the end of 1960-61. Indian ships now carry about 8 to 9 p.c. of India's overseas trade. During the Third Plan the additional tonnage proposed to be acquired will be 5·2 lakh GRT at a total cost of Rs. 119 crores.

These efforts are commendable. But there are certain difficulties. The capacity of the ship-building yard at Vishakapatnam is small and the cost of construction of ships is comparatively high on account of a number of factors. At the same time, purchase of ship from foreign countries requires heavy capital outlay which we can ill-afford. Moreover, there is a dearth of well-trained naval officers to man the ships.

We have also to face stiff competition from well-established foreign shipping lines with their large financial resources.

Air transport : It is the fastest form of transport and has been developed to some extent only after the Second World War. Before that there were of course one or two Indian companies, but the development was comparatively small. In 1948, the first external service between Bombay and London was opened by an Indian company, and there were a number of companies operating internal air services. By 1951 Indian companies operated 27 internal services.

In 1953, the Government of India decided to nationalise air transport, and two Corporations were set up, the Indian Airlines Corporation to operate internal service and the Air-India International for international services. In addition, several first class air-ports already exist in the country at Dum Dum, Santa Cruz and Palam, while there are about 75 aerodromes in different parts of the country, which are being maintained by the government. Facilities for technical training have also been provided, notably at Allahabad. The Third Five Year Plan proposed to spend Rs. 55 crores on the development of civil aviation.

Questions

1. Discuss the necessity of separating railway finance from the general budget of the country. Give a brief survey of the different conventions on the separation of railway finance.

2. Discuss how far the railway rates policy has hindered the growth of industries in India.

3. Describe the influence of the construction of railways on the economic life of India.

4. Evaluate the factors in favour of motor transport as against railways.

5. Discuss the problems of rail-road co-ordination. How far have the governments succeeded in co-ordinating them ?

6. Describe the efforts to build up a mercantile maine in the post-war period. What are the difficulties in its development ?

7. What is the present position of shipping in India ? Discuss the necessity of developing India's own mercantile marine.

8. Examine the present position and future possibilities of air transport in India.

CHAPTER 31 FOREIGN TRADE

The impact of the British rule, the occurrence of industrial revolution and the opening of the Suez Canal,—all these combined to produce a great change in the composition of India's foreign trade. Previously India used to export manufactured goods of fine quality and workmanship like cotton and silk piece-goods, made in her cottage industries and such commodities as salt-petre, indigo etc., and imported specie, and a number of miscellaneous manufactures. But towards the end of the 19th and the beginning of the 20ih century, her cottage industries declined with result that her imports consisted mainly of manufactured goods, while she began to export mainly raw materials like raw jute, raw cotton etc., and food crops. As before, bullion still continued to be imported in substantial quantities from abroad.

Foreign trade before 1939 : Upto the beginning of the Second World War, India's foreign trade retained, more or less, the same characteristics, though it varied in value and volume in different decades. One important characteristic of this period was the preponderance of primary commodities in her exports, and of manufactured consumer goods in imports. Thus in 1938-39, the item, raw materials, food, drink and tobacco formed 68 per cent of total exports, and manufactured goods formed 62 per cent of the imports. There was of course a tendency for the percentage of manufactured goods in imports to decrease over years on account of the adoption of the policy of discriminatng protection. The proportion of manufactured goods in imports had thus declined from 84 p.c. in 1920-21 to 62 p.c. in 1938-39, and that of raw materials had increased from 5 p.c. to 22 per cent during the same period. Moreover, while imports consisted of a large variety of goods, exports consisted of comparatively a few commodities like raw jute, raw cotton, tea, oil-seeds etc.

A second noticeable point was the fact that the U.K. constituted the best customer of Indian goods as well as the best supplier of imports. In 1938-39, the share of the U.K. amounted to 34·3 p.c. of India's exports and 39·5 p.c. of her imports. There was of course a tendency for the share of the U.K. to decline as her share in India's imports fell from 62·8 p.c. in 1909-14 to 39·5 p.c. in 1938-39.

Throughout this period, with a few exceptional years, India enjoyed a favourable balance of trade. The balance of trade was unfavourable only during the years 1920-21 and 1921-22. For some years during the world trade depression, the position was of course unfavourable, and it was the large exports of gold taking place in these years, which enabled the government to maintain the fixed value of the rupee-sterling ratio. The reasons for the existence of such a favourable balance of trade are well-known. India was a debtor country, having borrowed heavily from the U.K. throughout this period. A debtor country had to pay interest and repay part of its loans every year, and so it had to develop a favourable balance of trade to meet these payments. In addition, India had to transfer every year large sums of money on account of the "Home Charges" and other obligations to Great Britain, and her favourable balance of trade was partly utilised in this way. Thirdly, India used foreign shipping, banking and insurance services to a large extent, and she had to pay for these. Lastly, the most important factor was the steady demand for Indian exports in foreign countries. In 1920-22 the collapse of the first post-war boom in other countries, led to a serious decline in the demand for her exports, and this caused the balance of trade to become unfavourable. Similarly, in the thirties, the decline in the world demand for industrial raw materials led to a steep fall in the values of her exports and so to unfavourable balance of trade.

Trade during the second world war : During the second world war foreign trade was rigidly controlled as in every other country. Throughout these years, India enjoyed a continuous period of favourable balance of trade on account of the inability of the principal European and American countries to send goods to India, and partly on account of the heavy demand of the allied countries for war materials. During this period, some changes took place in the composition of trade. The proportion of manufactured goods in exports increased from 30 p.c. in 1938-39 to 44 p.c. in 1944-45, while that of raw materials declined from 45 p.c. to 31·7 p.c. during the same period. Similarly, in imports, the proportion of raw materials increased from 22 p.c. to 54 p.c. while the percentage of manufactured goods declined from 52 p.c. to 32 p.c. during the same period.

Foreign trade since the Partition : Since the achievement of independence in 1947, a number of events combined to affect the course

of foreign trade of this country. These are the partition of the country, the devaluation of the rupee, the impact of the Korean war, etc.

The partition of the country into two areas, India and Pakistan, affected the foreign trade of India in several ways. First, part of what was previously the internal trade of the country now figured in the foreign trade of India. Coal or cotton piecegoods sold in areas now included in Pakistan were formerly part of the internal trade of the country. Now they are regarded as the exports of India into Pakistan. Secondly, while almost all the cotton mills, or jute mills remained in India, the major portion of the areas growing raw cotton and raw jute came to be included in Pakistan. As a result, India had to import these from the latter, whereas previously India used to export large quantities of raw cotton and raw jute before 1947. Hence India's exports of those raw materials declined, while her imports increased by large amounts as she had to bring these raw materials from Pakistan. Similarly, India had to import foodgrains, while Pakistan remained a surplus country in food-grains.

The devaluation of the rupee in September, 1949, affected India's foreign trade in two ways. First, it gave a stimulus to exports, which increased considerably in the immediate post-devaluation period. Secondly, it led to a dispute with Pakistan which refused to devalue her currency. This resulted in a stoppage of all trade between India and Pakistan.

The outbreak of the Korean war in June, 1950, gave another upward thrust to our foreign trade. The intensified stockpiling of strategic materials led to a substantial rise in the demand for, and prices of, industrial raw materials. This caused considerable rise in the value of exports as well as imports. The total value of exports from India rose from Rs. 524 crores in 1950 to Rs. 742 crores in 1951, and that of imports from Rs. 508 crores to Rs. 774 crores during the same period.

The slump in prices which started from February, 1952 had its effect on foreign trade. With the progress of disinflation the value and volume of foreign trade became gradually adjusted to the changed situation. The volume of imports declined by 12 p.c. and prices by about 4 p.c., and the volume of exports fell by 10 p.c. as compared to the previous year (1951). In the meantime the country had successfully passed over the food crisis, and the increase in the domestic

production of food-grains led to a decline in food imports. Thus the balance of payments during 1953 recorded a surplus on current account of Rs. 59 crores as compared to the nominal surplus of Rs. 1·7 crores during 1952.

Characteristics of present-day foreign trade : During the post-war years certain broad changes have taken place in the character and composition of our foreign trade. In the first place, the percentage of manufactured goods in our export trade has increased from 38 p.c. in 1939-40 to 39 p.c. in 1959-60, while that of raw materials has declined from 43 p.c. to 18 p.c. during the same period. The same tendency is also present in the case of imports, where the percentage of manufactured goods declined from 56 p.c. in 1939-40 to 21 p.c. in 1959-60, and that of raw materials increased from 22 p.c. to 28 p.c. during the same period. This shows the impact of the progress of industrialisation achieved by the country, and of the policy of export promotion and import control. This is further borne out by the fact that of the total volume of imports, machinery of all kinds formed only 12 p.c. in 1938-39 and 22 p.c. in 1959-60.

Secondly, the impact of the partition of the country is evident from the fact that while in 1938-39, export of raw cotton formed 12 p.c. of the total exports, being second in the export trade in point of value, these formed only 2 p.c. of the total exports of 1959-60. Exports of raw jute which formed 7 p.c. of the total exports in 1938-39 virtually disappeared in 1956 and had been replaced by small imports. Imports of raw cotton formed only 5 p.c. of the total imports in 1938-39 as compared to 45 p.c. in 1959-60.

Thirdly, another noticeable feature is that our export trade is confined to only a few important commodities. Exports of jute manufactures, cotton manufactures, tea and hides and skins (both raw and tanned) accounted for more than 47 p.c. of the total exports in 1959-60.

Fourthly, as regards the regional distribution of trade, Great Britain still occupies a predominant position in our foreign trade, though her share is gradually decreasing. Thus exports from Great Britain formed 16·5 p.c. of the total Indian imports in 1962-63 as compared to 31 p.c. in 1938 and 27·5 p.c. in 1948 ; imports into Great Britain formed 23·6 p.c. of the total Indian exports in 1962-63 as compared to 34·6 p.c. in 1938 and 22·5 p.c. in 1948. On the other hand, the importance of the U.S.A. has increased considerably in recent

years. In 1938-39, that country purchased only 10 p.c. of our exports and supplied only 6 p.c. of imports. Whereas in 1962-63, the U.S.A. bought 16·8 p.c. of our exports and supplied 29·7 p.c. of our imports. Our trade with the Dollar area countries has improved to such an extent in 1953 that, as compared to a deficit of Rs. 111·2 crores in 1952 in our balance of trade with these countries, we achieved a surplus of Rs. 31·0 crores. On the other hand, the surplus in our balance of trade with the sterling area countries (excluding Pakistan) declined from Rs. 85 crores in 1952 to Rs. 43 crores in 1953. In 1951-52, our trade with the sterling area countries amounted to nearly 50% of our total trade : in 1959-60, the proportion has declined to 46.

Lastly, the most important change in the character of our foreign trade was the appearance of an adverse balance of trade. Prior to 1947, the balance of trade used to become adverse only in a few years. Whereas in the five years from 1948, the balance of trade became unfavourable in all these years. It should, however, be noted that though the balance of trade was adverse in all these years, the balance of payments on current account was positive in 1950 and 1953. What caused grave concern was the existence of large trade deficits in relation to the Dollar area countries, especially on account of the need for large-scale food imports. It was only in 1953 that we had a surplus on current account in relation to the Dollar area countries.

Causes of adverse balance of trade : A number of factors have been responsible for the recent adverse balance of trade, *viz.*, partition of the country, the need for large imports of foodgrains, the inflationary situation in the country, etc.

The partition of the country affected our balance of trade in many ways. It resulted in a reduction in our exports of raw cotton and raw jute and increased our need for imports of these commodities. Thus in 1938 our exports of raw cotton amounted to Rs. 23·93 crores, whereas imports of raw cotton were Rs. 11·07 crores. In 1951 imports of raw cotton amounted to Rs. 113·04 crores and exports to only Rs. 25·49 crores. Our exports of raw jute are now practically nominal, whereas in 1953 we imported raw jute worth Rs. 14·11 crores. Secondly, the increase in population and the decline in food production on account of natural calamities forced the government to import food-grains in large amounts, thus turning the balance of trade against us. In 1946

the value of grains, pulses and flour imported by us amounted to only Rs. 16·30 crores ; whereas in 1951, it amounted to Rs. 174·04 crores.

A third factor is the need to import machineries on a large-scale for the growing industries of our country. During the war it was not possible to carry out renewals and replacements of plant and equipment on account of the non-availability of capital goods from abroad. So we had to import machineries for replacements and renewals. In addition, planned development of large-scale projects called for imports of machinery from abroad. The total value of imports of machinery amounted to only Rs. 19·81 crores in 1938 as against Rs. 95·62 crores in 1951. So in spite of the cutting down of non-essential imports through the import control machinery, the volume of imports remained substantially high. Our exports are, however, meeting with considerable resistance in the world markets. For example, in 1953, though our exports increased in quantitative terms, export prices declined by a larger percentage than was the case with import prices. As a result, the total value of exports increased at lower rates or fell by larger amounts as compared to the changes in the total value of imports.

A developing economy will usually have to face large deficits in its balance of payments. To develop its industries rapidly, as we are doing now in India, the country will have to import capital goods on a large scale. Under-developed countries do not generally possess a capital-goods industry and so has to depend on imports of machinery at least at the initial stage. In addition, the increase in money incomes consequent on economic development, will lead to increasing demands for imports, both of consumers goods as well as food articles, the actual rate of increase depending on the marginal propensity to import and on the elasticity of the home production of foodgrains. At the same time, a smaller proportion of the domestic goods will be available for exports as the demand for raw materials and foodgrains increases within the country. The result is that while imports tend to rise, exports decline or increase at much lower rates. Hence the balance of trade is bound to be increasingly unfavourable. This is what is now happening in our country in the fifties.

Government measures to fight the adverse balance of trade : The government adopted a number of measures to solve the problem of

the adverse balance of trade. First, they have adopted import control measures, especially in relation to dollar imports. Imports could be brought in only under licence and attempts were made to cut down non-essential imports consistent with the requirements of the country. Secondly, the government adopted the policy of devaluation of the rupee in terms of gold and dollar in September, 1949, mainly to stimulate our exports to the Dollar area. In this it was successful to some extent. Thirdly, the government adopted a number of export promotion measures, such as the reduction of export duties on jute goods, on linseed and linseed oil, on tobacco seed oil, etc. A special organisation charged with the duty of export promotion has also been set up. Fourthly, attempts are being made to increase the domestic production of raw jute and raw cotton etc., so as to reduce our dependence on imports of these commodities. To a large extent this has been successful, and our imports of these commodities have declined considerably since 1953. Lastly, the various anti-inflationary measures like the raising of the Bank-rate in November, 1951, the change in the Reserve Bank's policy regarding the purchase of government securities, adoption of selective credit control measures etc. resulted in checking the rise in prices, and so have gone some way towards remedying the price disequilibrium.

Analysis of foreign trade by commodities : In this section we propose to study the principal commodities which are exported and imported.

Chief articles of exports : Among the principal export commodities, jute yarns and manufactures, tea, hides and skins (raw and tanned) and cotton yarns and manufactures etc. are more or less prominent.

Our exports of jute manufactures amounted to Rs. 182·85 crores in 1965-66. One item among jute manufactures, *i.e.*, hessian, is the best dollar earner. Prior to 1947, we also exported large quantities of raw jute. But this has practically been stopped and we became importers of this essential raw material. The growth in the domestic production of raw jute has enabled the industry to meet the foreign demand for jute manufactures.

Exports of *tea* amounted to Rs. 102·68 crores in 1965-66. The market for tea is mainly in Great Britain where demand sagged in

1952, leading to a crisis in the tea industry. Fortunately demand has revived again, helped to some extent by a reduction in the output of tea, and tea prices have registered a sharp rise.

Hides and skins are exported both in the raw and manufactured state. Exports of hides and skins (raw) amounted to Rs. 9·55 crores, and those of tanned hides and skins and leather amounted to Rs. 28·36 crores in 1965-66.

Exports of *cotton yarns and manufactures* amounted to Rs. 63·29 crores in 1965-66. These exports have grown in importance since the end of the Second World War, when the Indian mills succeeded in capturing many markets previously supported by Japanese cotton textiles. India has begun to export cotton piece-goods not only to the Asian countries, but even to the U. K. The Cotton Textiles Enquiry Committee (1954) has laid down a target of exports of cotton piece-goods at 1,000 m. yards. India also exports some raw cotton whose value was Rs. 13·09 crores. This is mostly of short-stapled variety.

Exports of *spices* amounted to Rs. 23·89 crores in 1965-66. Pepper is an important article of export, sold in countries of Europe and the U.S.A. In 1965-66, we exported pepper worth Rs. 16·85 crores. Pepper is a good dollar earner, and fetched dollars worth Rs. 6·57 crores in 1962-63. Recently the Spices Enquiry Committee appointed by the Government recommended the setting up of a Pepper Development Fund and other improvements to increase the exports of this commodity.

Tobacco worth Rs. 19·58 crores was exported in 1965-66. Great Britain is the principal buyer of tobacco. *Manganese Ore* worth Rs. 11·05 crores was exported in 1965-66. It is an important strategic material, and its demand has increased recently on account of the existence of the cold war.

We exported selected engineering goods such as sewing machines, electric fans, dry batteries, bicycles worth Rs. 4·40 crores in 1965-66.

India also exports sugar (11·64 crores in 1965-66), cashew nut (Rs. 27·40 crores in 1965-66), coal (Rs. 2·80 crores), iron ores (Rs. 42·10 crores), paper (Rs. 78·40 crores), leather and leather manufactures (Rs. 88·46 crores), mica (11·27 crores), iron and steel (Rs. 12·61 crores), etc.

Chief articles of import. The changes which have taken place in the structure of our import trade in the post-war years will be evident from the fact that the first place among imports is occupied by machinery. In 1965-66, India imported machinery worth Rs. 489·49 crores. This has become necessary on account of the need for replacement and renewals of old equipment and for the development of new industrial units.

Various kinds of *foodgrains* worth Rs. 309·61 crores were imported during 1965-66. Though we imported small quantities of foodgrains before 1939, these imports increased considerably in the post-war years on account of the growth of population, failure of crops and the partition of the country. India imported foodgrains worth Rs. 152·73 crores in 1952-53 and Rs. 218·71 crores in 1951-52 as against Rs. 63·65 crores in 1953-54.

The next important item is iron and steel whose imports amounted to Rs. 97·76 crores in 1965-66. This has become an important article of import on account of the development of the country.

The next major item is petroleum and petroleum products, and the value of these imports amounted to Rs. 68·35 crores in 1965-66. We also imported railway vehicles worth Rs. 24·87 crores and other transport equipment worth Rs. 45·02 crores in that year. Non-ferous metals worth Rs. 68·35 crores have also been imported. In addition. India imported chemicals worth Rs. 104·85 crores in 1965-66, cotton (raw and waste) worth Rs. 46·20 crores, paper and paper board (Rs. 13·15 crores), medicines (Rs. 8·16 crore), dyeing and tanning materials (Rs. 6·58 crores) etc. in 1965-66.

Export trade : Before the Second World War, the total value of exports from India was normally higher than the total value of imports. But the position has changed after the war. At the present moment, our exports are in general lower than the imports, and this has become the normal feature of our foreign trade. Not only that, but it seems that the exports have reached an almost stationary state. The total value of exports of merchandise was Rs. 609·41 crores in 1955-56, Rs. 612·52 crores in 1956-57, Rs. 621·31 crores in 1957-58, Rs. 580·30 crores in 1958-59, Rs. 648·83 crores in 1960-61, and Rs. 693·70 crores in 1962-63. In 1965-66 it has risen to Rs. 817·14 crores. For the first four years of the Second Plan the average value of our

exports was Rs. 608·5 crores. Moreover, India's share in the total export trade of the world amounted to 2·18 p.c. in 1948. From that figure it started to decline and it had come down to 1·3 p.c. in 1958.

Another characteristic of our export trade is that we depend on a small number of commodities for the export trade. Tea, jute manufactures, raw cotton and cotton manufactures, these three have been our traditional export commodities. In fact, the value of these exports formed about 51 p.c. of the total value of our exports in 1962-63. The other four traditional exports have been spices, hides and skins (raw and manufactured), tobacco and lac, and the value of these exports amounted to a little less than 10 p.c. of the total exports in 1962-63. But one encouraging feature is that our export trade is tending to become diversified, following the economic development of the country. Thus the total value of our three traditional exports has declined from 63·9 p.c. of the total export trade in 1948-49 to 55·9 p.c. in 1955-56, to 52 p.c. in 1958-59 and to 44 p.c. in 1965-66. New commodities are entering our export trade such as the engineering goods like sewing machines, fans etc. and the quantities of certain other older exports (such as iron ores, cashew nuts etc.) have tended to rise over the last decade.

The other encouraging feature has been the fact that during the last 4 years our export trade has increased by about Rs. 131 crores over that of 1962-63. In 1961-62, the total value of our exports amounted to Rs. 655 crores, and it had further risen to Rs. 686 crores in 1962-63 and this figure has been exceeded only during 1951-52 under the impact of the Korean boom. There has been an increase in the export of jute goods, cotton manufactures, our traditional exports, though those of tea and manganese ore have declined during this year. At the same time we have begun to export bicycles in sufficient numbers (Rs. 11 lakhs), and we are now exporting sewing machines even to the industrially advanced countries like the U.S.A.

Export promotion : The need for taking special measures for the expansion of exports is evident from the fact that we are running a large deficit in our balance of trade during the last decade. The average value of imports for the first 4 years of the Second Plan amounted to Rs. 1050 crores, while the average for exports was roughly Rs. 610 crores. The deficit would have much larger but for the fact that our imports are now rigidly restricted by the government. Such

strict control over non-developmental imports cannot be maintained indefinitely. Moreover, there is no reason to expect a serious decline in our imports in the near future. It may be argued when the programme of industrialisation of the country is completed, the need for importing machinery would diminish. But there will be increased demand for raw materials and intermediate products to sustain the industries. Moreover, as money incomes rise within the country, there will be more and more demand for new consumers goods. So the demand for imports may not decline at all, and may actually increase. For the present, foreign aid may enable us to meet the gap in our balance of trade. But this cannot go on for ever, and so it is essential that we should take steps to secure a considerable expansion in the export trade to meet the deficit in our balance of trade. Over and above these factors, the foreign debts that we are incurring at present would have to be paid off in course of time and the interest payments would also amount to large figures. The Third Plan has estimated that the payment of interest and the repayment of loans would require an amount of about Rs. 500 crores during the Third Plan period. It would be necessary to increase the exports in order to meet these additional payments. A plan for the expansion of exports should therefore form an integral part of any plan for the development of the country.

The Third Plan was drawn up on the assumption that our exports would have to be increased to an average of Rs. 690 crores during 1961-62 to 1965-66, and that we should aim at reaching the figure of Rs. 750 crores by 1965-66. To achieve this increase in exports, the government has adopted a number of steps during the last 3 or 4 years. Most of the controls over exports have been removed, and export duties on a number of commodities have been abolished or reduced to low levels. The government has also simplified the procedure for the repayment of the customs duties paid on imported raw materials used in the manufacture of exports. Special facilities and freight concessions are being given to help the movement of exports by rail and by sea. Licences for the imports of raw materials required in the production of exports are being freely given.

The government has also set up eleven export promotion councils whose main function is to devise measures for market research and improvement of marketing techniques. Commodity Boards such as the Tea Board, the Coffee Board and the Coir Board are paying more and

more attention to increase exports. A directorate of export promotion has also been organised to provide a variety of services to the exporters. In addition, the government is participating in international fairs and exhibitions on a large scale to popularise Indian exports and commercial representation abroad has been strengthened. Trade agreements have been concluded with 25 countries with facilities for rupee payments. Export bills have been included in the Bill Market scheme of the Reserve Bank of India with facilities for rediscounting.

The government has also set up an Export Risks Insurance Corporation to provide insurance against the risks of default by foreign buyers. An exporter will now be encouraged to grant liberal credit to the foreign buyers as any loss on non-payment or non-realisation will be guaranteed by this Corporation in return for small premia. Lastly, a State Trading Corporation has also been established to supplement the existing trading organisations, and to organise exports on an expanding basis and in particular commodities with particular countries.

All these measures have served to remove some of the difficulties faced by our exporters and to make them more export-conscious. But a good deal has to be done if the export targets of the Fourth Plan are to be realised in practice. There is a great need for the adoption of cost-reducing methods of production, improvement in quality and design, and the constant search for new markets. A most important aspect of export promotion relates to the marketing side. Our manufacturers have not paid sufficient attention to adapt their products to suit the changing consumer habits of the foreign buyers or to extend the market by developing new uses or varieties. Another factor hampering the development of our exports is the lack of integrity on the part of some of our exporters. Complaints are often heard about the fact that the goods supplied are not up to the standard of the samples originally sent to the foreign buyers. Little attention is paid to the maintenance of quality, to good and attractive packing, market surveys, publicity and the like. The best way to solve these defects is to organise the exporting firms in particular commodities into an Export House which would then be able to conduct intensive advertisement campaigns, to bring about conformity to samples, proper grading and standardisation etc.

Another essential need is to maintain prices at competitive levels. The world market is highly competitive and the foreign buyer has many alternative sources of supply from which he can buy. If the export

prices are high, the country will be unable to sell in the world markets. Hence the export producers would have always to be on guard and take steps to increase their efficiency of production and marketing and to reduce costs.

Last of all, it is necessary to examine the possibilities of expansion in respect to different commodities,—both in the short as well as the long run. Where there are good export possibilities, the Planning Commission should fix production targets after taking account of these possibilities. These targets should also take account of any likely increase in domestic consumption, as for example, with regard to the production of tea. The consumption of tea is increasing in the Indian market on account of the rising money incomes. The production target for tea should be fixed in such a manner that sufficient tea would be available for the export market after meeting the domestic demand. In a case where the output of a commodity cannot be adequately expanded, but there are good possibilities in the export markets, it may be necessary to take steps to restrict domestic consumption by fiscal and other measures. This may become necessary in the case of raw cotton, cotton textile manufactures, vegetable oils, etc.

It would, moreover, be necessary to search for new markets, and to find out new commodities. For example, there is considerable scope for expanding the sales of even our traditional exports in the U.S.S.R. and the East European countries. There is also a good possibility of increasing the exports of iron ore, lac, tobacco, and a number of engineering and miscellaneous goods and special studies should be made of these commodities.

Balance of trade : The table below gives the data relating to the balance of trade in merchandise during the 15 years since 1950-51. It will be found that in all these years the balance of trade was more or less unfavourable, being the least during 1950-51. This is however a post-war phenomenon. The balance of trade was favourable till 1946-47 with the exception of one year 1945-46.

The first year of the 1st Five Year Plan witnessed the highest deficit in the balance of trade due to an abnormal increase in the volume of imports. The deficit tended to decline thereafter and touched the bottom in the 4th year (1954-55). In the 5th year, the deficit had started to climb up, though it was still rather low by the standards of

the Second Plan. The total deficit in these 5 years amounted to a little over Rs. 600 crores.

The deficit has, however, tended to rise by large amounts during the Second Plan period, and in the first two years of this Plan, the aggregate deficit was almost equal to that of the earlier five years. The deficit touched the peak during 1957-58, after which it came down in the next 2 years.

TABLE I

BALANCE OF TRADE IN MERCHANDISE

(In crores of rupees)

Year	Exports	Imports	Balance of Trade
1950-51	600·65	650·22	— 49·58
1951-52	732·96	971·20	—238·24
1953-54	530·63	610·24	— 79·61
1955-56	608·90	774·25	—165·35
1956-57	612·52	832·45	—219·93
1958-59	580·30	856·18	—275·88
1960-61	642·07	1121·62	479·55
1961-62	660·58	1091·63	—431·05
1962-63	685·32	1131·48	—446·16
1963-64	793·24	1290·45	—497·21
1964-65	816·11	1313·61	—497·50
1965-66	805·28	1350·44	—545·16

Questions

1. Describe the nature of India's foreign trade, pointing out its chief characteristics.

2. Describe the principal features of India's foreign trade by commmodities.

3. Estimate the causes of India's adverse balance of payment in recent post-war years. What measures have been adopted to correct the adverse balance ?

4. What are the factors which have influenced India's balance of payments since the devaluation of 1949 ?

5. Discuss the changes that have taken place in the nature, volume and direction of India's foreign trade in the last decade.

6. What are the trends in India's exports and imports since 1951 ? Show how these trends reflect certain changes in the Indian economy.

7. Examine the need for, and the possibilities of export promotion during the Fourth Plan period.

CHAPTER 32

TRADE POLICY AND TRADE AGREEMENTS

Imperial preference : In the first half of the 19th century, the East India Company followed mainly the laissez faire policy in trade, tempered by some preference granted to British goods imported into India. Thus Regulation IV of 1815 provided that goods, produced in non-British countries, were to pay double the rates of duty levied on British goods, even if the non-British goods were carried in British ships. These preferential rates of duty were abolished in 1859, after the assumption of direct rule over India by the British Crown. From that year, upto 1923, commercial policy was dominated by free trade principles. In 1903, however. the Government of India was asked to join in a scheme of imperial preference. But it rejected the proposal as, in its opinion, the proposal was of doubtful value to India. However, in 1919, the Government granted preference to the empire countries and reduced by 10 p.c. the duty on the exports of hides and skins to these countries.

The question was considered by the Fiscal Commission of 1922, which recommended the adoption of a policy of discriminating protection. That Commission, while agreeing that "in its general features the analysis of the situation then (*i.e.,* in 1903) made holds good to day", recommended selective and discriminating preference provided that the requisite degree of protection to the Indian industry was maintained, and that this did not involve appreciable economic loss to India. Between 1923 and 1932 preference was granted to British goods only in two cases, *viz.,* iron and steel and cotton piece-goods. For example, the import duty on cotton piece-goods imported from Lancashire was reduced by 5 per cent.

Ottawa agreement, 1932 : In the meantime a fundamental change took place in the trade policy of Great Britain. Following the devaluation of sterling in September, 1931, the government of that country adopted the policy of protection and levied duties on all imports with the exception of imports from the empire countries, this exemption to last till November, 1932. In the meantime, an Imperial Economic Conference was called at Ottawa in Canada. India concluded an agreement, called Ottawa Agreement, under which she agreed to grant

preferential rates of duty on a large number of British goods in return for the grant of a similar preference for Indian goods in the British markets. The main reason which guided the Indian Delegation to conclude this Agreement was that in its absence India would have to face acute competition in the British markets as most of her competitors, (*i.e.* the other empire countries) had concluded such agreements and so would enjoy preferential rates of duty.

Though the Ottawa Agreement was ratified by the Indian legislature for 3 years, there was considerable criticism of the Agreement in the country. These critics argued that the fear of the loss of the British markets for Indian exports, if India did not join the scheme of imperial preference, was much exaggerated. Such loss would not be substantial. As against this India would have to grant preferential rates of duty on 163 classes of British goods. This preference could be granted either by reducing the duties levied on imports of British goods, those on non-British goods remaining the same : or by raising the duties on non-British goods, those on British goods remaining the same. If the first course was followed, (*i.e.* duty on British goods was reduced), there would be loss of customs revenue and a shrinkage in the margin of protection for Indian industries. If duties on non-British goods were raised, a larger rise in prices of imported goods would take place, and the poor Indian consumers would then have to bear a larger burden than would be the case in the absence of preference.

The supporters of the Agreement, however, argued that it had "a high insurance value." It provided a guarantee that Indian goods could not be ousted from the very valuable British markets. "It was no longer a question of what India stood to gain, but what she stood to lose." The majority of India's exports had to meet with considerable competition both from empire and non-empire countries. If Great Britain withdrew the preference from Indian goods, India would have to face a great loss.

The Ottawa Agreement was supplemented by the Iron and Steel Agreement of September, 1933, and by the *Mody-Lees Pact* or *the Bombay-Lancashire Agreement* of 1933. The latter was concluded between a British Textile Mission and the Bombay Millowners' Association, and provided for the grant of preferential rates of duty

for cotton piece-goods of Lancashire in the Indian market against the grant of certain preferences then enjoyed by British goods in Empire and other overseas markets to Indian cotton piece-goods. Lancashire also promised to make an attempt to use increasing quantities of Indian cotton. In 1935, a Supplementary *Indo-British Trade Agreement* was signed by the Government of India. This Agreement sought to lay down certain general principles to be followed regarding the treatment to be accorded to British goods competing with Indian goods when the Indian industry was to be granted protection. Thus under this Agreement British industrialists would be given the right to present their case before the Tariff Board enquiring into the question of the grant of protection to an Indian industry. This Agreement was not ratified by the Indian legislature, which also voted for the termination of the Ottawa Agreement. Though the Agreement was terminated in 1936, the preferences were, however. continued as a purely interim measure till the conclusion of a new agreement. This was done in 1939 when the Indo-British Trade Agreement was concluded. The Indian Legislative Assembly refused to ratify it. when it was certified by the Governor-General.

Indo-British Trade Agreement, 1939 : Under this Agreement India was granted, with two exceptions, all the preferences she enjoyed in the British market under the Ottawa Agreement. On the other hand, India granted preferences to British goods to only 20 tariff items, instead of 106 items. Secondly, the British government agreed to grant to India any tariff preferences granted to any of the British Dominions, and India, in return, agreed to grant to Great Britain any preferences she gave to any of the Dominions. Similarly, the governments of the British colonies agreed to grant to India preferences granted by them to other parts of the British Empire with certain exceptions against similar preferences to be granted by India. Thirdly. imports of British cotton piece-goods into Indian markets were linked under a sliding scale with the British imports of Indian cotton.

The second world war broke out within a few months of the conclusion of this Agreement. Since then India's trade has been governed by the method of import controls. Hence it is difficult to ascertain the effects of the working of this Agreement.

A review of Imperial Preference : Though begun earlier, the system of imperial preference had been in operation since 1932. What

has been the effects of the scheme on the internal economy of the country ? The question was examined by the Fiscal Commission of 1949-50 whose findings would now be discussed.

The Fiscal Commission took up the study of three charges that were usually brought against the system of imperial preference. First, it would mean loss of revenue from the customs duties ; secondly, it would mean smaller protection to the domestic industries ; and lastly, it would impose serious burden on the consumer.

Regarding the first point, if preference is granted by reducing the duty on imports of British goods, it would no doubt result in some loss of revenue from the customs as the British goods would pay import duties at lower rates. The Commission, after pointing out the difficulties in making a quantitative estimate of the probable loss of revenue, on account of the effects of the war, import control and changes in the tariff structure, however, endorsed the views of the Ministry of Finance that "the revenue implications of the preferential arrangements as they exist to-day are not of much importance."

Regarding the second point, it should be noted that both in the Ottawa Agreement and the Indo-British Trade Agreements, protected articles were kept out of their scope. So there was little risk of preference reducing the quantum of protection required by a domestic industry.

Lastly, it was also its opinion that from the nature of preferences granted to different articles these were hardly likely to impose any additional burden on the consumer.

It, however, appeared that between 1938-39 and 1948-49 India's share of the export market in preferred articles to Great Britain had fallen while the latter's share in the Indian market in preferred articles had remained satisfactory. India's policy in regard to preferences should, therefore, be reviewed in the light of this situation. The continuance or otherwise of the scheme of preference should be decided on the basis of mutual interests, after balancing all these considerations. India should, however, endeavour to follow a policy of abolishing or reducing preferences in return for tariff reductions on Indian goods by foreign countries.

Other pre-war Trade Agreements : India had entered into two more bilateral trade agreements before the last war—two with Japan and one with Burma.

The *Indo-Jap Trade Agreement*, first concluded in 1933, was formed to prevent cut-throat competition between Indian and Japanese cotton goods. The Indian cotton industry was unable to face Japanese competition and this agreement provided that in return for Japanese purchase of Indian raw cotton to the extent of at least 1 million bales per year, Japan would be entitled to export 325 million yards of cotton goods to India. The maximum quantity of cotton goods that Japan would be allowed to send to India would be 400 million yards, provided that she bought $1\frac{1}{2}$ m. bales of raw cotton from India. This agreement was renewed in 1937 with some modifications. It was later denounced by the Government of India as a protest against Japanese aggression.

The *Indo-Burma Trade Pact* was signed in 1941. When Burma was separated from India in 1937, it was provided that, as an interim measure, the two countries were to maintain free trade with each other until the end of March, 1941. Under this Pact, the two countries agreed to grant preference to the goods of other country. Indian goods would be granted a margin of preference in the Burmese market of not less than 10 p.c., over British goods and of not less than 15 p.c. over goods of other countries, in return for the same concessions granted to Burmese goods in Indian markets. Some goods would be allowed entry without any duty. Thus paper, coir, glassware etc., from India and wood and timber, iron and steel etc., from Burma would not have to pay any duty in the other country. As regards cotton piece goods, Burma would grant a preference of $7\frac{1}{2}$ p.c. over British goods and would not levy more than 10 p.c. duty on Indian piece-goods and would not increase the existing quota of Japanese piece-goods.

Post-war Trade Agreements : After the achievement of independence the Government of India has entered into trade agreements with a large number of countries like Pakistan, Sweden, Western Germany, Japan etc. The necessity for these agreements arose because of the fact that our balance of payments was in deficit with a large number of these countries. In a number of cases, Indian traders were not able to establish trade relations with these countries. In a few cases, the government undertook to sell certain commodities in these countries, where these would not be sold under normal conditions in exchange for other essential goods which these countries were in a position to supply to India. Barter agreements were also made with China, Argentina and one or two other countries. For example, the

Indo-Argentina Barter Agreement, concluded in 1953, provided for an exchange of 40,000 metric tons of hessian for Argentine wheat of equal value.

The value of these bilateral trade agreements should not be exaggerated. They might lead to some expansion in our exports, especially in countries with which we had previously no trade relation. They may also enable us to secure certain essential commodities which other countries with which we have trade relations, are not in a position to supply on account of (say) bottlenecks in production. Thus there is a possibility of some expansion in the total foreign trade of the country. But the greatest danger of these bilateral trade agreements is that they may lead to an artificial diversion of the foreign trade of these countries. But so long as the present system of import control or exchange control remains in different countries there may be no alternative to the conclusion of bilateral trade agreements in order to safeguard the position of Indian exports and to ensure the ready availability of essential imports.

India and the International Trade Organisation : At the conclusion of the Second World War there was a general conviction that the maintenance of peace would be much facilitated if there was mutual co-operation in the field of trade and employment between different countries. With this end in view, an International Conference on Trade and Employment was convened and it met at Havana in Cuba. This Conference recommended the setting up of an International Trade Organisation (ITO) and drew up a Charter laying down the constitution and functions of the organisation. This Charter was signed by 54 nations, subject to ratification by individual countries.

The objectives of the Charter were to reduce tariffs aid other barriers to trade and to eliminate discriminatory trade treatment and so, by increasing the opportunities for trade, enable countries to abstain from the adoption of measures which would disrupt world trade. Secondly, it was meant to facilitate through consultation and co-operation the solution of problem relating to international trade in the fields of employment, economic development, commercial policy, etc., and thus to increase income, demand, production, consumption and exchange of goods.

The chief organ of the ITO will be the conference of all member-nations which will normally meet once a year. The conference would

elect an Executive Board of 18 members to carry on day-to-day business, subject to the final sanction of the conference.

The Charter required member-nations to negotiate for the substantial reduction of tariffs and elimination of preferences, subject, of course, to certain exceptions. Another article of the Charter stated the general rule against prohibition of imports or exports and quotas in respect of them. A sub-section of this article, however, contained exceptions permitting import quotas under certain circumstances. Another article laid down that any member might maintain existing quotas for the development or reconstruction of particular industries provided that such quotas were not discriminatory. Quotas were permitted when necessary to meet the balance of payments difficulties. Each member was to grant most favoured nation treatment to all other countries on equal terms, subject to some exceptions. For example, India was permitted to continue existing preferences with Great Britain and the colonies, though the ultimate objective would be the elimination of such preferences on a mutually advantageous basis. There is nothing in the Charter to debar a member-country from developing its industries under the shelter of protective duties. But it attempts to fit in some of the protective measures needed for developmental purposes as closely as possible with the principles of multilateral trading.

The question whether India should ratify the Charter or not was referred by the government to the Fiscal Commission of 1949-50. The Commission listed the objections which had been raised against the Charter. The most serious objection is that the ratification of the Charter might hamper India in its task of developing her resources. Under the Charter it would be necessary for India to approach the ITO at every step for permission to adopt measures to develop her industries. The Commission found that this criticism was too general. The Charter permits the adoption of protective measures such as tariffs and subsidies and the limitations to the use of these measures were by no means serious. The use of quantitative restrictions was of course much more restricted. But the Charter includes so many exceptions to this article that in the short period the employment of quantitative restrictions was possible in all *bona fide* cases without prior reference to the I.T.O. Thus the provisions of the Charter did not impose any serious limitations on India's freedom to mould its commercial policy in the interests of its domestic economy. So the Commission recommended that India should ratify

the Charter provided that other countries of major importance such as Great Britain and the U.S.A. ratified it, and that the economic conditions in the country at the time of ratification justified the adoption of this course.

As very few countries have ratified the Charter, there has been no necessity for India to take up consideration of this question.

India and the G.A.T.T.: As there was some delay in the setting up of the I.T.O., 23 countries met in the meantime at Geneva in 1947 and drew up a General Agreement on Tariffs and Trade, known shortly as the G.A.T.T. Under this agreement the member-countries agreed to some reductions in the tariff on each other's goods. One important feature of the concessions received and granted was its multilateral application. A concession received or granted through negotiation with any country was to be immediately extended to other participating countries also. The needs of individual countries and their industries were taken into account and the negotiations were conducted on a selective, product-to-product basis, thus ensuring flexibility. At Geneva 123 sets of bilateral negotiations were completed, covering two-thirds of the import trade of the participating countries. A second conference was held at Annexy in France and third at Torquay in England.

The question of the ratification of the G.A.T.T. was also referred to the Fiscal Commission, which recommended that India should continue to adhere to the G.A.T.T. India has signed this Agreement.

Questions

1. Do you think that it will be to the best interest of India that she should now be included in any scheme of imperial preference ? Give reasons for your answer.

2. What objections have been raised against the Indian ratification of the I.T.O. Charter ? Do you recommend such ratification ?

3. Give a brief review of some of the trade agreements made by India with other countries. Do you think that these agreements confer great benefits on Indian trade ?

CHAPTER 33

CURRENCY AND EXCHANGE UPTO 1939

The history of the Indian currency system is an interesting study. During the last century, India passed through a variety of monetary system of which the gold exchange standard provided an outstanding example. In this chapter we propose to study the history of Indian currency upto the eve of the Second World War. The present-day problem of the currency system will be studied in a later chapter.

When the East India Company gradually extended their sway over different parts of India, there were a bewildering variety of currency systems prevalent in the country. There were sliver currencies and gold coins circulating side by side. In order to bring about some uniformity the Company passed the Currency Act of 1835, which provided for the free coinage of silver rupees containing 180 grains of silver (11/12th fine). This Act also authorised the coinage of gold if required by the public, and gold mohurs were accepted at the treasuries at the ratio of 15½ silver coin for one gold coin.

Fall in the ratio and its consequences : By 1873 the Indian currency consisted mainly of silver rupees in which there was free coinage. The notification authorising the acceptance of gold mohurs was withdrawn in 1852, and since that year India was virtually on the silver standard. But things began to change from 1873 on account of the continuous fall in the price of silver. The discovery of new silver mines and the demonetisation of silver by a large number of European countries caused a fall in the price of silver, which declined from 60d. per oz. in 1872 to 29d. per oz. in 1894. As there was free coinage of silver in India, every fall in the price of silver meant a fall in the gold value of the rupee. Since sterling, the British currency, was on the gold standard, a fall in the price of silver led to a decline in the rupee-sterling ratio, which fell from 22·7d. in 1872 to 14·5d. per rupee in 1894. This continuous decline in the rupee-sterling ratio created certain difficulties for the government which had to make large payments in sterling every year. A fall in the rupee-sterling ratio meant that the government had to pay larger sums in rupees to buy the same amount of sterling. Moreover, the government could not know beforehand how many rupees it

would require to buy the required amount of sterling. The preparation of the budget thus became a difficult task.

Herschell Committee (1892) : To escape from these difficulties, the Government of India at first tried for a number of years to promote the system of international bimetallism. But these efforts proved ineffective on account of the unwillingness of the major European countries to adopt bimetallism. So in 1892 the government appointed a Committee under the presidency of Lord Harschell to examine the currency situation. The Herschell Committee recommended the closing of the mints to the free coinage of silver with the ultimate purpose of adopting the gold standard. In accordance with these recommendations, the government suspended the free coinage of silver, and henceforth only the government had the right to coin silver rupees. For some years, no attempt was made to coin rupees, as a result of which there was a relative shortage in the supply of rupee coins as trade and industry expanded in the country. The value of rupees began to increase and with it the sterling value of the rupee rose gradually until it became equal to 16d. per rupee in 1898.

Fowler Committee (1898): The Government then appointed another Committee known as the Fowler Committee, which recommended the fixation of the rupee-sterling ratio at 16d. per rupee, the existing ratio. The ultimate goal should be the establishment of gold standard with gold currency in circulation, and for this purpose they recommended that the British sovereign (at that time a gold coin) should be declared a legal tender, and that the mint should be thrown open for the coinage of gold, and that though the government should continue to exchange rupees for gold coins, rupees should not be coined until the proportion of gold in the currency was found to exceed the needs of the public. The Committee further recommended that when the government would begin to coin silver rupees, any profits from such coinage should be taken to a special reserve to be called the Gold Standard Reserve.

Towards Gold Exchange Standard : All these recommendations were accepted by the government. Sovereigns were declared legal tender in 1899. But it was not found possible to establish a branch of the Royal Mint in India, on account of the opposition of the British Treasury. Indian treasury offices were asked to issue sovereigns and half-sovereigns to the public as far as possible. But extensive famines all over India resulted in a return of these gold coins back from

circulation and the government took it to be a sign that the public did not want gold coins. Famine conditions led to increased demand for rupees, to meet which the government began to coin rupees, and to set apart the profits in a special reserve. The Gold Standard Reserve thus came into existence, and in spite of the opposition of the Government of India, the Secretary of State decided to keep this Reserve invested in London in sterling securities.

The ratio was henceforth kept fixed at 1s. 4d. per rupee (*i.e.*, Rs. 15 to the £). As India had a favourable balance of trade in this period, there was no difficulty in maintaining this rate of exchange. On the other hand, gold was shipped to India to liquidate her favourable balance. As this gold had again to be shipped back by the government to London to be kept in the Gold Standard Reserve and the Paper Currency Reserve, it was considered needlessly expensive. So the Secretary of State decided to sell Council Drafts without limit at 1s. 4½d. per rupee, to be encashed in India in terms of rupees. All merchants who had to export gold to India to pay for the goods purchased from the latter sold this gold to the Secretary of State for Council Drafts (or Council Bills), and sent these Drafts to the Indian sellers who obtained payment in rupees in exchange of these Drafts from the Government of India. Thus so long as the Secretary of State sold Council Drafts without limit at 1s. 4½d. per rupee, the ratio could not rise above this point.

This went on so long as the balance of trade remained favourable. But in 1907, India experienced an adverse balance of trade on account of a number of factors, such as the failure of crops. the American recession etc. As a result, there was a heavy demand for sterling in exchange of rupees on the part of Indian importers, and this tended to cause the rate of exchange to fall below 1s. 4d. per rupee. After some hesitation, the Government began to sell Reverse Council Drafts to Indian importers who paid for these in rupees, and sent them to their London creditors. The latter presented the Drafts to the Secretary of State who paid them off in sterling from the two Currency Reserves. These Reverse Councils were sold at the rate of 1s. $3\frac{29}{32}$ d. per rupee, and in this way the lower limit to the ratio was fixed.

The result of the adoption of all these measures was the establishment of the gold exchange standard, and not the gold standard as originally recommended by the Fowler Committee.

Gold Exchange Standard : Gold exchange standard is said to exist in a country when gold coins do not circulate within the country, but the local currency, which consists of coins of other metals or paper currency, can be converted into gold at a fixed ratio, this gold being made available at a foreign centre where the gold reserves are kept. Thus in a gold exchange standard country, (*a*) the local currency consists of paper currency notes or of coins of silver and other metals. Gold coins do not circulate within that country. (*b*) But the monetary authorities undertake to give gold in exchange for local currency at a fixed ratio. (*c*) Gold is not, however, given within the country in exchange for local currency, but at some foreign centre, and (*d*) the authorities keep the gold reserves at this foreign centre to facilitate the payment of gold in exchange of local currency. This standard is different from gold standard primarily in one respect. In gold standard gold is available from monetary authorities within the country either in the form of gold coins or gold bullion, whereas under gold exchange standard it is available outside the country.

India was on the gold exchange standard during the period 1900-1917. The local currency consisted of silver rupees and paper currency notes. Gold coins did not circulate within the country, but the government undertook to give sterling in London in exchange for rupees in India at the rate of 1s. 4d. per rupee. Since Great Britain was on gold standard throughout this period, sterling, the British currency, was convertible into gold, and hence the undertaking to give sterling meant the same thing as that to give gold. Lastly, the various currency reserves, the Gold Standard Reserve and the Paper Currency Reserve, were kept mainly in London, a foreign centre.

Mechanism of the standard : The rate of exchange between the rupee and the sterling was kept fixed at 1s. 4d. per rupee in the following way. First, the rate was prevented from rising above this figure by the Secretary of State undertaking to sell Council Drafts without limit at the rate of 1s. 4½d. per rupee. The London merchants who had payments to make to India and so required rupees could buy these Drafts from the Secretary of State and send these to their Indian creditors who presented them to the Indian Treasuries and received payments in rupees. So long as these Drafts were sold in unlimited amounts at fixed rates, the ratio could not rise above 1s. 4½d. per rupee.

Secondly, the fall of the ratio was prevented by the sale of Reverse Council Drafts. These Drafts were sold by the Government of India to any one in India in exchange for rupees at the rate of 1s. $3\frac{29}{32}$d. per rupee. These were encashable in sterling in London, and were paid off by the Secretary of State out of the various currency reserves.

Merits and demerits : It has been claimed on behalf of the gold exchange standard that it worked in the same way as the gold standard, while it meant a great economy in the use of gold. As gold coins did not circulate within the country, the monetary authorities would not have to buy gold for coinage purposes. Secondly, the same gold reserves kept in London would serve as the basis of the monetary systems in Great Britain and India, and so the operation of this standard would lessen the pressure on the gold supply of the world.

These two benefits that were claimed were, however, mutually incompatible with each other. If any economy in the use of gold reserves was secured, this standard could not function as in gold standard. When India had a favourable balance of trade, the Secretary of State sold Council Drafts to meet the demand for rupees. This led to an increase in rupee circulation and so to a rise in prices in India. When the Secretary of State sold Council Drafts, the proceeds were credited to the various Reserves kept in London. The balances standing to the credit of the Secretary of State increased, and if the Bank of England did not make any distinction between these balances and other balances, it would not take any steps to curtail the supply of money in circulation. Prices would not fall in England as they would have done under gold standard. If, however, the Bank of England regarded the balances of the Secretary of State as not forming part of the British currency system, an increase in the former would mean a fall in the supply of money available for use in England. In this case, there would be no economy in the use of gold, but British prices would fall as in the gold standard.

There were also other defects of this system related to its working in India. These were due primarily to the absence of any Central Bank in India, as a result of which the management of the standard was left to officials. These officials did not always possess the necessary training for the management of currency and as they were not in touch with the trade and market conditions, their management of the standard was often miscalculated. There was, moreover, a dangerous division of control of currency and credit. The government officials controlled the currency

and there was no authority to exercise control over the banking system. As a result, the banking system was divorced from currency, and this could not lead to their smooth working of the standard.

Break-down of the standard : The break-down of the gold exchange standard was due primarily to the rise in the price of silver which took place during the first world war. During this war, India enjoyed a highly favourable balance of trade to liquidate which there was a large demand for rupees. It was, therefore, necessary to coin rupees. But in the meantime, the price of silver jumped up by leaps and bounds owing to the shortage in the supply of silver bullion and a very keen world demand for that metal. Most of the belligerent countries prohibited the export of precious metals including silver and this led to an acute shortage in the supply of silver in the world. The price of silver rose continuously till August, 1917 when it was no longer economically possible to sell Council Drafts at 1s. 4d. per rupee. With the rise in the price of silver, the value of the silver bullion contained in the rupee threatened to rise above one rupee, and there was a danger that the whole of the rupee coinage would be melted down and the silver sold as bullion. The government was, therefore, compelled to raise the rate of exchange to 17d. per rupee in August, 1917, and shortly afterwards gave up all attempts to fix the rupee-sterling ratio, which rose gradually to 2s. 4d. per rupee in December, 1919. It meant a break-down of the gold exchange standard.

Babington-Smith Committee (1919) : With the end of the first world war, the Government appointed a Committee known as the Babington-Smith Committee to make recommendations as to the future of the Indian currency. The Committee anticipated that the price of silver would remain at a very high level after the war. So they thought that the value of the rupee should be kept at a high figure in order to retain its token character. They were also against linking the rupee with sterling. Sterling was then off gold, and so its value tended to fluctuate in terms of gold. If the rupee was linked with sterling, it would have to share the violent fluctuations of the sterling. So the Committee recommended the fixation of the value of the rupee at 2s. gold. Such a high rate would have the additional advantage as it would arrest the rising tendency of prices and would also cause some saving in home charges.

Failure of the 2s. gold ratio : These recommendations were accepted by the government which took steps to keep the ratio fixed at

2s. gold. As sterling was depreciated in terms of gold, this meant the fixing of the rupee-sterling ratio at somewhere between 2s. 10d. to 2s. 2d. per rupee, depending the depreciation of the sterling. This attempt proved a failure on account of a number of circumstances, the most important of which was the tendency towards an adverse balance of trade which set in from January, 1920. This meant a serious decline in the demand for rupees, and there was also considerable speculation in exchange. Commercial firms and importers hastened to make their remittances to London to avail themselves of this high rate. There was, therefore, a heavy demand for sterling and the government found it impossible to keep the ratio at 2s. gold. Thereupon it attempted to maintain the ratio at 2s. sterling, which also proved a failure. At last the attempt to fix the exchange was given up from 28th September 1920. after causing a net loss of Rs. 35 crores in exchange transactions. The rate of exchange fell immediately until it touched the low point of 1s. 3.13/32d. per rupee in July, 1921.

Hilton-Young Commission (1925-26) : The post-war adverse balance of trade continued till 1921-22 after which there was some recovery in trade. This stopped the decline in the rupee-sterling ratio which began to rise thereafter with the appearance of the favourable balance of trade. In the meantime the budget was balanced and some contraction of the currency was carried out. The result was an upward tendency of the exchange, which rose to 1s. 6d. per rupee in October, 1924. Meanwhile sterling appreciated in terms of gold, and was finally put on the gold standard at the old parity. The Indian exchange also reached 1s. 6d. gold, and in August. 1925, the Government appointed the Hilton-Young Commission to examine and report on Indian currency and exchange. The report of the Commission was issued in July, 1926. The Hilton-Young Commission made three important recommendations. It advocated the adoption of the gold bullion standard, the setting up of a Reserve Bank of India and the fixing of the ratio at 1s. 6d. per rupee. We propose to discuss them one by one.

Gold Bullion Standard : From a long time there was a persistent demand in India for the adoption of a good standard with a gold currency in active circulation. Several witnesses made this demand before the Commission. and one or two definite schemes to that effect were submitted in evidence. The Commission rejected this demand on the ground that the attempt to introduce gold currency in India would put a heavy

pressure on the world's supply of gold which was threatening to become short in relation to existing demand. This would mean a rise in gold prices and a fall in silver prices, and this was bound to bring about depression throughout the world, whose adverse effects India could not expect to escape. If the object of these proposals was to secure the automatic working of the currency system and to inspire public confidence, it could equally be secured under the gold bullion standard.

The Commission, therefore, recommended the adoption of the gold bullion standard. Under this standard the gold sovereign would cease to be the legal tender in India where the local currency would consist of rupees and paper currency notes. These would be convertible into gold bars containing 400 oz. of gold (1067 tollas) at the rate of Rs. 21-3-10 p. per tollah. The Paper Currency and Gold Standard Reserves should be amalgamated and should form the basis for the successful working of the standard.

These proposals were accepted by the government which passed an Act in 1927. Under that Act the price of gold was fixed at Rs. 21-3-10 p. per tollah at the rate of 1s. 6d. per rupee, and the currency authorities were placed under an obligation to buy and sell gold bars containing 40 tollahs at that price. A gold bar containing 400 oz. of gold as recommended by the Commission was considered too high for a poor country like India, and so the amount was lowered to 40 tollahs. Sovereigns and half-sovereigns ceased to be legal tender, but were accepted at the treasuries at the rate of Rs. 13-2-4 p. sovereign. India remained on this standard till September, 1931, when following England's departure from gold standard, India suspended the gold bullion standard.

Reserve Bank of India: The Commission felt that many of the difficulties of the Indian currency system could be remedied if a central bank was established in the country. The Imperial Bank of India was then performing some of the central banking functions. But the Commission rightly felt that as the Imperial Bank was the largest commercial bank, it would mean a great loss to the country if it was to be converted into a central bank. So they recommended the establishment of a separate central bank in the name of the Reserve Bank of India. This Bank was to be a purely shareholders' Bank with shares subscribed by private persons or institutions. The majority of the Board of Directors would be elected by the shareholders, and the government would nominate only a small number of Directors. The Governor of the Bank was

to be appointed by the government on the recommendation of the Board of Directors. No member of any legislature would have the right to sit on the Board of Directors of the Bank. The Bank would be entrusted with the usual central banking functions, *e.g.*, the sole right to issue paper currency notes, the management of the government's balances and of the public debt, right to act as banker to other joint-stock banks which would be required to keep certain percentages of their deposits with the Bank, purchase and sale of gold at fixed prices, management of the exchanges etc.

There was a violent controversy in the country over these recommendations, especially those relating to the provisions requiring the Bank to be purely shareholder's bank. A large section of opinion wanted a State Bank. A Bill embodying these recommendations was introduced by the government in the legislature. But it was finally abandoned after passing through a number of vicissitudes on account of the strenuous opposition of the Congress Party and other non-officials.

1s. 6d. *vs.* 1s. 4d. controversy : The Hilton-Young Commission decided by a majority to recommend the fixation of the ratio at 1s. 6d. gold per rupee, which was the prevailing rate during the sittings of the Commission. One member, Sir Purshottamdas Thakurdas, advocated a return to the old ratio, 1s. 4d. per rupee in his minority report. Since then, the country passed through one of the most bitter and prolonged controversy over the question of the proper ratio at which to fix the value of the rupee. The controversy broke immediately with the publication of the report and lasted till the outbreak of the Second World War.

A review of this controversy should naturally start from the points made in the two reports of the Commission. The majority preferred the 1s. 6d. ratio on the ground that it was the *de facto* ratio which was being maintained for more than a year. Prices and wages had become adjusted to this higher ratio, and the course of foreign trade did not also show any sign that the ratio was over-valued. India continued to enjoy a favourable balance of trade, and there was no sign that imports were being specially stimulated or exports checked which would have been the case if the ratio was over-valued. With regard to contracts, the majority of commercial contracts were usually concluded for short periods when the ratio was already 1s. 6d., or at least not 1s. 4d. per rupee. Rates of land revenue were of course fixed at a time when the ratio was 1s. 4d. But the great rise in prices since 1919 had materially lightened

the burden of land revenue, and even after the fall in prices caused by the higher ratio, prices were higher than when land revenue was fixed. In view of these factors, if an attempt was to be made to go back to 1s. 4d. ratio, it would raise prices by 12½ p.c., and so arbitrarily reduce the real wages of labour, and increase the burden of "home charges." The lower ratio would mean that the government would have to find more rupees to pay for the "home charges", and this might upset their budget and result in the postponement or the abolition of provincial contributions.

The minority report, on the other hand, disputed the fact of adjustment of prices and wages to the higher ratio. There was no evidence that the general level of wages had fallen after the rise in the rate of exchange. The higher ratio would mean increasing the burden of agricultural debts to the extent of 12½ per cent. The adverse effects of a reversion to the 1s. 4d. ratio on a small section of the population must not be allowed more weight than the suffering which the higher ratio was imposing upon the agricultural classes who formed the vast majority. The effect of a reversion to 1s. 4d. ratio on the public finances should not be exaggerated. The government would of course have to find more rupees to pay for the "home charge". but it would also receive more revenue if the country escaped depression which would be brought about by the attempt to maintain the higher ratio. It was well-known that the higher ratio was being maintained through the continuous deflation of the currency. Lastly, the country had become so much accustomed to the 1s. 4d. ratio which had remained in force from 1898 to 1917, that it would mean almost like a breach of established standards to depart from this ratio.

In spite of the considerable opposition in the country, the government fixed the ratio legally in 1927 by passing an Act to that effect. This, however, did not put an end to the controversy which flared up from time to time—on different occasions, for example, with the beginning of the world trade depression in 1929, the passage of the Reserve Bank Bill in the legislature in 1933-34, the devaluation of some European currencies in 1936, the recession and weakening of the ratio in 1937 etc. The onset of the depression after 1929 or the recession of 1937 led to a considerable decline in India's foreign trade, which became unfavourable. As a result, the demand for sterling increased, making it difficult for the authorities to maintain the ratio at 1s. 6d. per rupee.

On both these occasions a large section of opinion demanded devaluation of the rupee to 1s. 4d. per rupee on the ground that the rupee was over-valued at the higher ratio. The considerable export of gold which took place was taken to be a symptom of disequilibrium in the balance of trade, to cure which a reversion to the lower ratio was advocated. To the argument that the rupee was over-valued at 1s. 6d. ratio, it was pointed out that with the devaluation of the sterling, the rupee which was linked with sterling was also devalued in terms of gold and so any tendency to over-valuation had disappeared after 1931. But the extent of the devaluation of the rupee in terms of gold was considerably less than that of many other currencies.

Sterling Exchange Standard (1931-1946): The next important event took place on September 21, 1931, when Great Britain had to give up the gold standard. The government decided to follow in the footsteps of sterling, and the provision requiring the currency authorities to sell gold bars in exchange for rupees was suspended. Henceforth the rupee was linked with sterling instead of with gold. In other words, India adopted the sterling exchange standard.

The sterling exchange standard is so called because the value of the rupee was kept fixed in terms of the sterling at the ratio of 1s. 6d. per rupee, the authorities undertaking to buy or sell sterling without limit at fixed rates. The immediate consequence was a rise in the price of gold and export of gold from India in large quantities.

This linking of the rupee with sterling came in for a good deal of criticism. It was argued that this meant that the rupee would have to share in the fluctuations and depreciation of sterling in terms of gold. It was quite possible that the natural level of exchange for England might not necessarily be the natural level for India. There is undoubtedly some truth in this contention. But against this one must remember that the alternative to the sterling exchange standard was either gold standard or an independent currency system. In 1931 and subsequent years, India was not in a position to adopt gold standard, as during these years almost all the countries of the world were forced off the gold standard. India could have managed an independent currency standard without any fixed link with either gold or sterling. But India had to meet large payments in sterling every year, and the greater part of her foreign trade was conducted in terms of sterling. An independent rupee would have caused budgetary difficulties as the government could not

have known beforehand how many rupees it would have to set apart for meeting the sterling obligations. The merchants engaged in foreign trade would also have had to face the same uncertainties on account of the fluctuations of the rupee in terms of sterling. Taking everything into consideration the adoption of the sterling exchange standard was not after all an unwise choice in the nineteen thirties.

Gold exports : The departure of Great Britain from gold standard and the linking of the rupee with sterling were followed by the export of gold from India on a large scale. Before 1931 India was primarily an importer of gold. Indeed she was always regarded as a sink for precious metals. But between September 1931 and January, 1940, India exported gold to the value of Rs. 351·4 crores.

It is necessary at this stage to distinguish between the two phenomena,—the rise in the price of gold and the export of gold. The depreciation of sterling in terms of gold and the linking of the rupee with sterling led to a considerable rise in the price of gold in the Indian market. From Rs. 21-3-10 p. per tollah on 20th September, 1931, the price of gold rose gradually to Rs. 31-10-6p. in December, 1932. Such a high price, induced many persons to sell gold. The prevailing economic distress in the rural areas on account of the depression led to what was called the "distress sale" of gold. But these causes did not explain the export of gold from India. Export of gold from India took place because the price of gold rose at a faster rate in the world's markets than it did in India. As a result, gold was exported from India for sale in the world's markets, at higher prices.

These gold exports were a god-sent to the government from many points of view. Between 1929 and 1931 India's balance of trade tended to become adverse, and the government was finding it extremely difficult to maintain the ratio at 1s. 6d. per rupee. The gold exports eased the pressure on the exchanges and the government was able not only to maintain the rupee ratio, but also to purchase large sums of sterling (*i.e.*, the proceeds of the gold exports) for meeting its sterling obligations. The Currency Reserve which were previously depleted on account of sales of sterling or reverse councils, were greatly strengthened because of the supply of abundant sterling.

A large section of Indian opinion, however, wanted to put an embargo on the export of gold. Or in the alternative they demanded

that the government and the Reserve Bank should buy this gold from the market to prevent its export. This would strengthen the reserve of the Reserve Bank of India. An embargo on gold exports would have depressed gold prices and would have harmed the interests of the distressed sellers of gold. The Reserve Bank could of course have bought, if not the whole, but at least a part of this gold in order to strengthen its reserves. But the government argued that this would have meant that the Reserve Bank was undertaking speculative transactions in gold. If gold prices declined in the future, the Reserve Bank would be involved in heavy losses, having earlier purchased gold at much higher prices.

The only other major event before the war was the establishment of the Reserve Bank of India from April, 1935. This will be discussed in the chapter on the banking system.

Questions

1. How did the value of silver influence the currency system of India during the period between (*a*) 1873-1898 ; (*b*) 1914-1919 ?

2. Explain the origin and development of the Gold Exchange Standard. Indicate the causes of its break-down during the First World War.

3. "A Gold Exchange Standard cannot provide an efficient remedy for the defects of the existing system of Indian currency." Discuss.

4. Describe the main features of the gold bullion standard and discuss its suitability for India.

5. Describe the circumstances leading to the linking of the rupee with sterling. What are the effects of such linking upon trade and industry ?

Describe the main features of the sterling exchange standard of India. What are its merits and defects ?

6. Account for the unusually large export of gold from India since 1931. Examine its advantages and disadvantages and state if you are prepared to impose any restrictions on such exports.

CHAPTER 34

CURRENCY AND EXCHANGE 1939-1966

On the eve of the Second World War (September, 1939), India was on the sterling exchange standard with the rupee linked to sterling at the rate of 1s. 6d. per rupee. The Reserve Bank of India had been established, and had already succeeded in solving the problem of the large differences in the money rates which existed in India.

The declaration of the war in September, 1939 was followed by a speculative rise in prices, which was, however, kept in check after a few months. But as bad war news began to come in, the people became nervous and there was a tendency to hoard rupee coins, and even small coins. Notes were being presented to the Reserve Bank for conversion into silver coins which were hoarded. In the month of June, 1940 when the news of the fall of France came, notes to the value of more than Rs. 15 crores were presented for conversion. Between June and August there was a record return of notes from circulation to the extent of about Rs. 22 crores.

To cope with this situation, the Reserve Bank began to ration the supply of rupee coins, and the government issued a Rule under the Defence of India Act, making it an offence for any person to acquire coins in excess of his personal or business requirements. On June 24, 1940, the Government of India issued one-rupee notes which were declared as equivalent to rupee coins. During the first world war the rise in the price of silver caused many difficulties and there was a danger that all rupee coins might be melted down and sold as silver bullion in the market. To prevent such a situation from arising during this war. the government adopted a number of measures. The old rupee coins, containing 160 grains of silver, were withdrawn from circulation, and in their place new coins containing only 90 grains of silver were issued. Silver half-rupee and four-anna pieces were also withdrawn from circulation and replaced by coins containing half the amount of silver. Similarly, a new pice coin containing a circular cut inside was issued to forestall any danger due to a possible rise in the price of copper. The Reserve Bank was also authorised to issue two-rupee notes from February, 1943. Gradually in course of time the panic hoarding of coins passed away, and the Reserve Bank was able to meet the demand for the absorption of coins of all kinds.

Another noticeable tendency was the large expansion in currency and bank deposits which took place with the rising tempo of the war. In September, 1937, the total volume of notes in circulation amounted to Rs. 196·14 crores. It rose to Rs. 1147·14 crores in the same month of 1945, *i.e.* an increase of Rs. 951 crores.

TABLE I

Month		Total volume of notes in circulation
September	1939	Rs. 232·10 crores
"	1940	Rs. 196·14 "
"	1941	Rs. 284·29 "
"	1942	Rs. 284·07 "
"	1943	Rs. 759·75 "
"	1944	Rs. 937·08 "
"	1945	Rs. 1147·14 "

This was done under the exigencies of war finance, and the notes were issued against mainly sterling securities. The value of sterling securities held in the Issue Department of the Reserve Bank increased from Rs. 60·50 crores in September, 1939 to Rs. 1042·33 crores in the same month of 1945, an increase of Rs. 981·83 crores, which was more than the increase in the volume of notes. As against this the value of rupee securities increased from Rs. 37·38 crores to Rs. 57·84 crores, *i.e.*, by only Rs. 20·46 crores. In September, 1939, sterling securities kept in the reserve amounted to only 30.8 p.c. of the note issue ; they amounted to 90·8 p.c. in September, 1945.

The same expansion took place in regard to the deposits of the scheduled banks. The total deposits of these banks increased from Rs. 232·33 crores in September, 1939 to Rs. 897·58 crores in the same month of 1945, *i.e.* an increase of Rs. 665·25 crores.

As a result of these operations, the total money supply with the public increased from Rs. 341·68 crores in September, 1939 to Rs 1961·38 crores in September, 1945. While money supply with the public increased at this rate, there took place a considerable rise in the general price level. The Economic Adviser's general index of wholesale prices rose from an average of 125·6 in 1939-40 to 245·0 in 1945-46.

The expansion in currency and deposits and the rise in prices in India and some other countries is illustrated in the following table published in the Reserve Bank's Report on Currency and Finance, 1945-46.

Indices of average monthly note circulation, demand deposits and wholesale prices.

(Index—July 39=100.)

		1939	1941	1943	1945 (Last quarter)
India	Notes	102	152	416	686
	Notes	101	144	319	509
	Notes	105	139	307	280
U.K.	Deposits	103	128	190	263
	Deposits	101	152	198	263
	Deposits	102	155	166	173
U.S.A.	Prices	102	151	316	538
	Prices	103	137	185	221
	Prices	102	116	137	143

Thus it is evident that the increase in note circulation, deposits and wholesale prices proceeded at higher rates in India as compared to those in the U.K., and the U.S.A.

One welcome feature was the fact that the accumulation of sterling balances on a large scale enabled the Government of India to repatriate the major portion of the sterling debts. The process of repatriation began from 1937, and the pace was accelerated during the war.

Thus the total face-value of sterling debts repatriated during 1937-38 amounted to £2·99m., in the seven years from 1939 to 1945-46, the total of sterling debts repatriated amounted to £320·13 m. at the cost of Rs. 425·23 crores. This has meant the virtual wiping out of our sterling debts.

From 1945 to 1947 : Almost the same tendencies continued since the end of the war to the date of the partition of the country. The average note circulation increased from Rs. 1147 14 crores in September, 1945 to Rs. 1193·37 crores on the 14th August, 1947. The value of sterling securities kept in the Issue Department of the Reserve

Bank of India increased from Rs. 1042·33 crores to Rs. 1135·33 crores during the same period, while the value of rupee securities remained steady at Rs. 57·84 crores throughout these months. The total deposits of the scheduled banks also increased from Rs. 714·13 crores in September, 1945 to Rs. 857·23 crores on the 15th August, 1947. The Economic Adviser's General Index rose from 242·2 in September, 1945 to 299·3 in August, 1947. The period, therefore, witnessed the continuation of the same inflationary trend which had its origin in the exigencies of war finance in India.

The most noticeable event during this period was the establishment of the two international institutions—the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBRD). As an original member of the IMF, the Government of India adopted certain technical changes in the currency system. Previously the value of the rupee was fixed only in terms of sterling. Henceforth the par value of the rupee was fixed at the rate of 1s. 6d. per rupee in terms of dollar or gold. The value of the rupee was fixed at 331 rupee per 100 dollars, *i.e.*, 30·23 cents per rupee. In terms of gold it was fixed at 0·268601 grams of fine gold. The Reserve Bank of India was authorised to buy or sell other foreign currencies in addition to sterling and to keep other foreign securities in the Paper Currency Reserve of the Issue Department.

The I.M.F. and India : With the abolition of the gold standard in the thirties of this century, all countries were on paper currency standard. Unless different countries maintained reasonable stability in the rates of exchange. large fluctuations in these rates would paralyse the course of international trade. To prevent such a chaotic state of affairs, the government of the countries at war with Germany and Japan decided to set up an organisation known as the International Monetary Fund. One of the main functions of that institution is to help the member-countries to stabilise rates of exchange and when necessary, to bring about orderly adjustment of changes in exchange rates. Each member-country is required to notify the IMF the rate of exchange between its currency and gold or dollar. The member is expected to conduct its foreign transactions on the basis of this exchange rate. To that extent the existence of the IMF will lead to stability of exchange rates. But unlike gold standard, these rates are not fixed for ever. If any country finds that in view of certain important changes in her economy, the

maintenance of the existing rate of exchange would lead to "fundamental disequilibrium", it will be entitled to change its exchange rate with the permission of the authorities of the IMF. In that way adjustments in the rates of exchange are to be brought about, not through the unilateral action of a country, but through international agreement. Lastly, in order that short-period fluctuations in its balance of payment may not force a country to change its rates of exchange, there are provisions under which the IMF would extend short-term credits to member-countries in balance-of-payments difficulties, subject to certain conditions.

India is one of the original members of the IMF, and is one of the permanent members of the Board of Governors of the Fund. Her membership of the IMF resulted in certain changes in the currency system and in the operations of the Reserve Bank of India. The most important change is the delinking of the rupee from sterling. The par value of the rupee was fixed in terms of gold or dollar, *i.e.*, 0·268601 grams of fine gold or 30·23 cents per rupee. Whereas previously the Reserve Bank was required to buy and sell only sterling among the foreign currencies, it is now placed under obligation to buy or sell foreign currencies at rates determined by the Government from time to time. These provisions have led to the legal termination of the link of the rupee with sterling. The rupee has now emerged as an independent currency directly linked to the currencies of all countries of the world, and not through sterling as was the case before 1947.

One or two other changes have also been made in the Reserve Bank Act to carry out India's obligation as a member of the IMF. Under the original Reserve Bank Act, the Bank was required to keep a reserve equal to not less than 40 p.c. of the value of the notes issued in the form of gold coin or bullion and sterling securities. This provision has now been changed, and the expression "foreign securities" has been substituted for "sterling securities." The Reserve Bank is now able to buy and sell all foreign currencies and the securities issued by the government of any country outside India which is a member of the IMF, and to hold them in the Issue Department as reserves against the paper currency. A minor change has been made with regard to the buying and selling rates for sterling. According to the provisions of the constitution of the IMF the maximum and minimum rates for exchange transactions between the currencies of the member-countries are not to differ more than one per cent. Under the Reserve Bank Act, the Bank was placed

under an obligation to buy or sell sterling at rates not below 1s. $5\frac{44}{64}$d. or above 1s. $6\frac{3}{16}$d. per rupee. As the rates were more than one per cent above or below the per value of the rupee, these were changed to 1s. $5\frac{55}{64}$d. (the lowest) and 1s. $6\frac{9}{46}$d. (the highest) per rupee.

India has also taken advantage of the provisions regarding the grant of short-term creditors by the IMF. She has borrowed, from time to time, considerable sums of dollars in order to meet the deficit in her balance of payment on current account.

Partition of the country and the currency arrangements : The Partition of the country into two dominions on the 15th August, 1947, created a number of problems for the currency authorities. Pending the establishment by the Government of Pakistan of machinery to regulate currency and banking, the Pakistan (Monetary System and Reserve Bank) Order was promulgated on the 14th August, 1947. The aim of this Order was to provide for the maintenance of a unified monetary system for the two Dominions till 30th September, 1948. The terms of this Order laid down that the Reserve Bank of India was to remain as bankers to the Government of Pakistan. It was to have the sole right to issue notes in Pakistan upto 30th September, 1948. The Bank was, however, to issue, after March 31st, 1948, distinctive bank notes inscribed with the words, "Government of Pakistan." These notes were legal tender only in Pakistan. Indian rupees and subsidiary coins were also to continue to be legal tender in Pakistan for such period or periods, not later than one year from the introduction of corresponding Pakistani coins. This Order was later amended providing that the Reserve Bank would continue as the currency authority in Pakistan upto 30th June, 1948, instead of 30th September, 1948. Arrangements were also made to determine the share of Pakistan in the assets of the Reserve Bank of India.

The Government of Pakistan set up the State Bank of Pakistan on 1st July, 1948, and from that date the Reserve Bank ceased to be the currency authority in Pakistan. The Reserve Bank's offices at Karachi, Lahore and Dacca were taken over by the State Bank of Pakistan. That Bank also took over all outstanding liabilities in respect of inscribed Pakistani notes, and accordingly, assets of the Reserve Bank in the Issue Department of the value of Rs. 51·57 crores were handed over to the State Bank. In the meantime the Indian notes in circulation in Pakistan were gradually withdrawn from circulation in that country, and handed

over to the Reserve Bank against the transfer of assets of equal value to Pakistan. The total amount of Indian notes returned from circulation in Pakistan and the Reserve Bank purchased Indian notes worth Rs. 127·17 crores in 1948-49. Under the orders of the Government of Pakistan, all Indian notes and coins ceased to be legal tender in that country with effect from 1st September, 1950.

Upto 20th September, 1949, there was parity between the Indian and Pakistani rupees. There was an agreement between the two Governments that the value of the rupee was not to be changed except after mutual consultation with each other. Following the devaluation of the sterling, the Government of India also decided, on 20th September, 1949, to devalue the Indian rupee in terms of gold and dollar. This decision was not accepted by Pakistan, which refused to devalue its currency. The value of the Indian rupee thus became equal to 21·00 cents per rupee, while that of the Pakistani rupee remained at the old level, *i.e.*, 33·23 cents per rupee. The breach between the currency systems of these two neighbours was, therefore, complete.

The 1949 devaluation of the rupee : The position with regard to our balance of payments was causing anxiety since the end of the war. The continuing deficit in the balance of payments led to a large decline in the sterling balances of the Reserve Bank, which fell from Rs. 1523 crores in August, 1947 to Rs. 781 crores in September, 1949. Devaluation was forced on this country as a result of happenings in Great Britain and other sterling area countries. In the post-war years Great Britain was finding it extremely difficult to meet the so-called "Dollar gap." That country had to import large quantities of goods from the dollar areas, while its exports could not be expanded to the desirable extent. The existence of inflation and the high cost of production of British goods prevented a considerable expansion in exports. As a result, Great Britain had to use up her gold and dollar reserves to meet the dollar gap. On 18th September, the British Government announced its decision to devalue the sterling in terms of dollar from the rate, \$4·40 to the £, to \$2·80 to the £. Sterling was thus devalued by 30·5 p.c. at a stroke. This was followed by a large number of other countries, both within and outside the sterling area. Even Canada, a dollar area country, devalued its currency by 10 p.c.

Faced with this situation, the Government of India also decided to follow suit, and announced, on the 19th September, its decision to devalue the rupee by the same percentage, *i.e.*, 30·5 p.c. The new ratio that was fixed was 0·18662 grains of fine gold per rupee in terms of gold or 20·94 cents in terms of dollar. The value of the rupee was kept fixed in terms of sterling at 1s. 6d. per rupee. This ratio became effective from the 21st September, as banks were closed before that date.

Reasons for devaluation. The Government of India gave a number of reasons for their decision to devaluate. One was the fact that the major portion of India's foreign trade was conducted in terms of sterling, and the sterling area countries which had devalued their currencies constituted our best customers. Had we refused to devaluate, the value of the rupee would have risen in terms of sterling, and the prices of Indian goods would have increased in the sterling area countries. This would have led to a decline in our exports to these countries, creating fresh problems for our balance of payments position. Secondly, most of the sterling area countries were also the principal competitors of our exports in foreign markets. For example, Ceylon is the most important competitor of Indian tea in the British market. As Ceylon had devalued her currency, non-devaluation by India would have meant a rise in the prices of Indian tea in the British market, while the price of Ceylon tea would have remained at the old levels. Indian tea would, then, have to face serious competition. Non-devaluation by India would have led to the loss of export markets.

Moreover, devaluation was supposed to help India to sell more goods in the dollar markets. India was facing a persistent dollar gap in her balance of payments, and devaluation, by cheapening Indian goods in dollar markets, might enable her to bridge the dollar gap.

One serious disadvantage that followed devaluation was the fact that India had to pay higher prices for the foodstuffs imported from the dollar areas. The prices of American machinery and other essential goods also rose, thereby imposing greater burden on the industries which had to import these things.

Effects of devaluation. The immediate effects of devaluation on the balance of payments were favourable. As against a deficit of Rs. 175·9 crores in the first nine months of the year, the last quarter showed a surplus of Rs. 29·4 crores. Exports showed a record increase for the quarter of nearly 38 p.c. over the previous quarter, the volume index

reaching 92·9, the highest figure for the post-war period. Part of this increase in exports was no doubt caused by deferred purchase as importers in the dollar countries had postponed their normal purchases in anticipation of devaluation. But there was no doubt that the devaluation of the rupee enabled Indian exporters to sell larger quantities both in the dollar area and sterling area countries. Exports to the dollar area countries rose steeply from an annual rate of Rs. 106·8 crores in the third quarter of 1949 to Rs. 173·2 crores in the last quarter of that year. In the sterling area countries India did not of course enjoy any price advantage. But the devaluation of the rupee led, in a number of these countries, to a substitution of commodities from the dollar areas or commodities with a high dollar content, by Indian exports.

It should, however, be noted that this improvement in the balance of payments after devaluation was due not only to the increase in exports, but also to a decline in imports, brought about mainly by a policy of rigid import control. Following the recommendations of the Commonwealth Finance Ministers' Conference, governments of the Commonwealth countries agreed to cut down imports from the dollar areas by at least 25 p.c. The results of this policy were obtained in the last quarter of the year.

This improvement in the balance of trade did not, however, continue on the same scale in the first six months of 1950. There was a net deficit in the trade balance for this period, though the position was much better when compared to the same period of 1949. This slow rate of improvement in exports was due primarily to low level of exports of jute manufactures whose production declined substantially. Pakistan's policy of non-devaluation led to the cessation of trade between the two countries, as a result of which the supply of raw jute became extremely scarce in the Indian market. and this was the most important reason for lower production and smaller exports of jute goods.

Devaluation gave an upward thrust to the prices as would be evident from the general index of prices which increased from 389·0 in August, 1949 to 395·6 in June, 1950 when the Korean war broke out. The largest increase took place in miscellaneous index which rose from 541·6 to 692·0 during the same period, and in the index of industrial raw materials which registered an increase of 30 points.

In the second half of 1950 the entire position was changed on account of the development of boom conditions throughout the world

under the stimulus of the outbreak of the Korean war and the stock-piling of the essential raw materials by the U.S.A. It was no longer possible to observe separately the effects of devaluation on the balance of payments or prices.

On the whole it cannot be said that this particular devaluation of the rupee exercised any material influence over the balance of payments except in the immediate period. The balance of trade was favourable, after of course a considerable period, in the last quarter of 1949 and the first quarter of 1950, after devaluation in September, 1949. But in the second quarter of 1950 (April to June), the balance of trade had again turned adverse, the net deficit being of the order of Rs. 20·5 crores. The total value of exports which rose from Rs. 102·1 crores in July to September 1949 to Rs. 133·3 crores in the next 3 months fell to Rs. 129·4 crores in the first quarter and to Rs. 112·5 crores in the second quarter of 1950. Even then part of this improvement in the balance of trade had to be ascribed to the severe restrictions imposed on imports. Thus devaluation of the rupee failed to provide any solution for the "intractable problem" of "the comparative inelasticity of India's exports".

The 1966 devaluation of the rupee : A glance at the balance of payments position for the last decade and a half will show an extremely serious state of affairs. In 1950-51, India's foreign exchange reserve amounted to Rs. 951·41 crores, which seemed quite ample according to our needs. But by the end of the Second Plan the reserves had dwindled to Rs. 303·61 crores. In each of the 5 years of the Third Plan, the deficit in our balance of trade was never less than Rs. 430 crores, and in 1965-66, the deficit amounted to Rs. 545·16 crores. Our exports of merchandise, after rising from Rs. 685 crores in 1962-63 to Rs. 816 crores in 1964-65, declined to Rs. 805 crores in the next year. So we had to borrow heavily from the IMF,—Rs. 119 lakhs in 1961-62, Rs. 47·6 lakhs in 1964-65 and Rs. 65·46 lakhs in 1965-66. Domestic prices had risen by more than 80 p.c. since 1952-53. Over the Third Plan period the weekly index of general price level had risen by 35·2 p.c., on top of a rise by 30 p.c. during the Second Plan period. In the meantime most of the foreign aid had been frozen after the outbreak of the three-weeks' war with Pakistan. In the meantime a World Bank Mission that was visiting and exploring the state of affairs in the Indian economy, suggested that the time had come, in view of the above-mentioned circumstances,

to bring the value of the rupee in equilibrium with its value in the domestic market. The free exchange value of the rupee had fallen to very low figures in terms of the dollar and the sterling, and a large clandestine trade in gold was being carried on, taking advantage of the gap between the official value of the rupee and its value in the price exchange markets.

All these factors led to the Government of India's decision to devalue the rupee on June, 1966 by 36·5 p.c. The new value of the rupee was fixed at Rs. 7·50 per dollar and Rs. 20 per pound. This was done to bring the external value of the rupee into more equilibrium with the domestic value in the first place, and to provide a stimulus to the exports. There is no doubt that the exports have proved to be almost stagnant, increasing by snail's pace. The most important reason for such a state of affairs was the rise in domestic prices and costs, which has resulted in pricing the exports out of the foreign markets. Devaluation will provide some remedy for this disparity between domestic prices and costs and foreign prices and so increase the competitive position of the export industries.

Devaluation will of course raise the prices of imported goods, among which the most important are the foodgrains and kerosene. As a rise in the prices of these two will adversely affect the slender budget of the poor who constitute the vast majority of the people, the government decided to sell these at former prices, meeting the differences between the import prices and the domestic prices through the payment of subsidy in the case of foodgrains and a lowering of excise duties in the case of imported oil. As the exporters are likely to receive sudden increase in their prices, the government levied export duties at varying rates, partly to mop up a part of the windfall gains of the exporters and partly to make up for the loss of revenue consequent on the lowering of the excise duties on imported oil. In addition, the government gave a promise to adopt suitable measures for restraining prices from rising after devaluation and so nullifying the effects of that measure. It was also decided to liberalise the imports of raw materials and spare parts in order to provide a boost to industrial production. As industrial production was almost being slowed down on account of the difficulty of importing the necessary raw materials and spare parts, this liberalisation was expected to lead to larger industrial production, which might offset any tendency towards rising prices. The affected

industries would be able to utilise their excess capacity fully and to step up the production of manufactures. Devaluation is also expected to check the outflow of foreign exchange through smuggling and other illegal means like the sale of travellers' cheque in the unofficial markets etc.

This announcement regarding devaluation has led to a big controversy as to the merits of the measure. The facts relating to our balance of payments situation, dwindling foreign exchange reserves, the rather large increase in prices, the fall in the value of the rupee in the unofficial markets are well-known. But these facts have been present from a long period, and if devaluation was not regarded as a proper remedy for these things in the earlier occasions, nothing has happened recently to induce us to adopt this measure of doubtful benefit. Exports are no doubt increasing very slowly. But a large number of economists were doubtful whether devaluation would result in increased exports. In the first place, in their opinion, the elasticities of foreign demands for our traditional exports were not of such a nature as to lead to larger total exchange earnings. The newer exports are too insignificant to be relied upon to provide us with the necessary increase in foreign exchange earnings. In the meantime, imports would be more expensive, and as imports consisted mostly of capital equipment, devaluation was likely to raise costs of manufactures and of the planned projects. It has been estimated that the cost of the Fourth Plan, estimated at Rs. 20,500 crores at pre-devaluation prices, would go up to at least Rs. 25,000 crores after devaluation. Any likely rise in exports was unlikely to provide us with the necessary foreign exchange earnings. On the other hand, devaluation is likely to lead to a further rise in prices, which the government would be unable to restrain, as it had so far failed to prevent prices from rising. There is as yet no sign that devaluation, carried out on the advice of the World Bank would be followed by a larger inflow of foreign aid. In fact, there is nothing in devaluation itself which is likely to lead to a large flow of foreign capital into the country, unless the foreign governments agree to relax a little. If prices rise again, as they have again started doing so, devaluation will yield no benefit, and may have to be followed by further devaluations. There is no doubt that we would have to carry out devaluation sooner or later. But that is only

a palliative. The real remedies have to go far deeper. We must learn to prune our ambition, to abstain from deficit-financing and to adopt the necessary measures to scotch the inflationary rise in prices.

Questions

1. Describe the effects of the last war on Indian currency.

2. Explain the causes that led to the expansion of Indian currency during the World War II.

3. Discuss the present position of the rupee in the Indian monetary system. What modifications have been introduced by India's adherence to the I.M.F.?

4. Describe the chief features of the I.M F., and say how far its membership has been beneficial or otherwise to India.

5. What circumstances led to the devaluation of the rupee in September, 1949 ? What were the immediate consequences of devaluation ?

6. Discuss the arguments for and against the devaluation of the rupee.

7. Discuss the present position of the rupee in the International Money Market. Are you in favour of revaluing it ?

8. Explain the main feature of the monetary system of India.

CHAPTER 35

THE RESERVE BANK OF INDIA AND THE MONEY MARKET

At the present moment in the vast majority of countries, the principal monetary authority is the central bank. This bank is usually entrusted with the sole right to issue paper currency notes and other forms of circulating media, to hold the currency and foreign exchange reserves and to maintain the foreign value of the currency, in addition to conducting the banking business of the government and regulating the rate of creation of credit by other banks. This bank, therefore, occupies a pivotal position in the money market, controlling the rate of the flow of currency and credit into that market. In this chapter we propose to study the operations of the Reserve Bank of India, which is the central bank of this country.

History of the growth of the Reserve Bank of India : Inspired by the example of the Bank of England, a number of proposals were made for the establishment of a central bank in India in the early days of the rule of the East India Company, without, of course, much effect. The proposal took a concrete shape in the report of the Chamberlain Commission of 1914, where the late Lord Keynes wrote a memorandum advocating the establishment of a State Bank in India, whose constitution and functions were also discussed by him in details. Nothing was done during the first world war, and after its end, an Act was passed which amalgamated the three Presidency Banks and established the Imperial Bank of India. This Bank, predominantly a commercial bank, was entrusted with certain central banking functions. It managed the government's banking business, gave occasional loans and advances to other banks and acted as an instrument for the issue of emergency currency during the busy seasons.

The question of the establishment of a full-fledged central bank was taken up by the Hilton-Young Commission of 1925-26. That Commission rejected the proposal to convert the Imperial Bank into a central bank. It recommended the setting up of a Reserve Bank of India charged with the usual central banking functions. That Bank was, however, to be organised as a private shareholders' bank, free from all sorts of political pressure and independent of the government. The latter would have only the right to nominate a number of Directors. A Bill to this effect was introduced by the government in the Indian legislature,

where the proposal to establish a shareholders' bank met with serious opposition. After passing through several vicissitudes, the Reserve Bank of India Bill was finally dropped by the government as the opinion held by the majority in the legislature was at variance with that of the government. The whole question was again taken up by at the Round Table Conferences held in London when it was laid down that before further constitutional reforms could be introduced, a properly constituted Reserve Bank was to be established and working in India. Accordingly another Conference was held in London for drawing up an agreed constitution for the Reserve Bank of India. A Bill embodying the recommendations of this Conference was introduced and passed into law in 1934, and the Reserve Bank of India started its career from the 1st April, 1935.

The Reserve Bank of India : *Its composition.* Under the original Act the Reserve Bank began as a private shareholders' bank with a paid-up capital of Rs. 5 crores, divided into fully paid up shares of Rs. 100 each. The whole of India was divided into five circles, *viz.*, Bombay, Calcutta, Madras, Delhi and Rangoon, having each a separate list of shareholders residing in these regions. No shareholder could hold shares in excess of the total nominal value of Rs. 20,000, and while the holding of five shares entitled one to vote, no shareholder could cast more than 10 votes, whatever might be the size of his holdings.

The affairs of the Bank were to be managed by a Central Board of Directors, and five local Boards. The Central Board consisted of 16 members including a Governor and one or two Deputy Governors nominated by the government on the recommendation of the Central Board, four Directors nominated by the government, eight Directors elected by the shareholders and one official nominated by the government. There was a Local Board in each of the five circles, consisting of five Directors elected by the shareholders and three Directors nominated by the Central Board.

This was changed in 1948 when the Reserve Bank was nationalised by the government. All shares were bought by the government which paid compensation to the shareholders. The Central Board of Directors now consists of 19 members, all of whom are nominated by the government. The four local Boards consist of 4 to 5 members, all being nominated by the Central Government.

The Governor is the Chief Executive of the Bank and the Local Boards conduct such business as are referred to them by the Central Board.

Like the Bank of England, the Reserve Bank has also two Departments, the Issue Department and the Banking Department. The former is responsible for the issue of paper currency notes and must hold adequate reserves in the forms prescribed by law. The Banking Department performs all other functions of the Bank. The Bank is also required under the statute to maintain a separate Agricultural Credit Department charged with the function of studying all questions pertaining to agricultural credit and co-ordinating the operations of the Bank in connection with the grant of agricultural credit.

Functions. Like all other central banks, the Reserve Bank of India has been entrusted with the following functions, *viz.*, (*a*) to have the sole right to issue paper currency notes subject to the keeping of reserves as laid down in the Act, (*b*) to act as the banker to the government, holding its balances, managing its debts and granting its loans as required, (c) to hold the reserves of other banks granting them loans and advances or rediscounting bills of exchange presented by them, (*d*) to maintain the external value of the rupee by the purchase and sale of foreign exchange at rates determined by the government, (*e*) to publish a Bank Rate and conduct open market operations for the control of the money market, (f) to manage the clearing house operations and to perform all other kinds of banking business not prohibited by law. It cannot pay any interest on any deposits accepted by it, nor can it lend to anybody with the exception of the government and the scheduled banks except under emergency conditions. We shall next discuss these functions in detail.

First, the Reserve Bank has the *sole right to issue paper currency notes* in India. These notes are of the value of Rs. 2, Rs. 5, Rs. 10, Rs. 100 and above, and are full legal tender in India. They are convertible on demand into rupees. It should be remembered that one rupee notes were regarded as equivalent to rupee coins. The Bank has to keep the full value of the notes issued in reserves, consisting of gold coin or bullion, foreign securities, rupee coins, rupee securities, and bills of exchange rediscountable by itself in the following proportions. The value of gold and foreign securities must not ordinarily fall below Rs. 200 crores, and the value of the gold must never fall below Rs. 115 crores.

Secondly, the Bank acts as a *banker to the central and state governments.* The balances of these governments are deposited with the Bank which also grants ways and means advances to them as required from time to time. These advances must be repaid within 90 days. The Bank also manages the public debt. It floats these loans, makes arrangement for the payment of interest and repayment of capital.

Thirdly, it also acts as a *banker to other banks.* Commercial banks whose paid-up capital and reserves amount to Rs. 5 lakhs are entitled to become a "scheduled bank" of the Reserve Bank of India. Every scheduled bank has certain obligations to the Reserve Bank and enjoys certain privileges. It has to maintain a balance with the Reserve Bank equal to 3 p.c. of its current account and fixed deposits. The Reserve Bank has been authorised to raise these reserve ratios upto 15 p.c. for purposes of controlling credit. It has to submit a weekly balance-sheet to the Reserve Bank. In return, it is entitled to borrow from the latter. It can take loans and advances, repayable on demand, or for a period not exceeding 90 days against trustee securities, gold or silver, or eligible bills of exchange or its own promissory notes supported by documents of title to goods. It can also rediscount bills of exchange drawn on and payable in India, arising out of *bonafide* commercial transactions, bearing two or more good signatures, one of which shall be that of a scheduled bank and maturing within 90 days, or bills of exchange drawn or issued for the purpose of financing seasonal agricultural operations or the marketing of crops and maturing within 15 months.*

Under the Banking Regulation Act of 1949, non-scheduled banks are also required to maintain cash reserves with themselves or with the Reserve Bank in the same proportions as in the case of a scheduled bank and to submit weekly returns of their balance-sheets.

The same Act has granted large powers of control over all banks to the Reserve Bank of India. It can determine the lending policies of banks, prohibit particular types of transactions, inspect the books and accounts of any bank, approve the opening of branches etc.

In addition to the ordinary commercial banks, the Reserve Bank has also been authorised to deal with the State Co-operative Banks or State Finance Corporations. It may grant loans and advances to these

* This period was previously fixed at 9 months. It was extended to 15 months in 1951.

institutions on the same terms as in the case of commercial banks. It may also grant to the State Co-operative Banks medium-term credit for agricultural purposes repayable within a period not being less than 15 months and not of exceeding 5 years provided that such loans and advances are guaranteed by the State government. The total amount of such medium-term loans at any time shall not exceed Rs. 5 crores.

Fourthly, the Bank is also entrusted with the task of *maintaining the foreign value of the rupee.* Originally it was laid down that the Bank was to buy or sell sterling to the scheduled banks in amounts of not less than one lakh of rupees at rates varying between 1s. 63/16d per rupee to 1s. 5 49/64d. per rupee. After India becomes a member of the I.M.F., this was changed. The Bank is now placed under obligation to buy and sell all foreign currencies in amounts of not less than one lakh of rupees at rates determined by the Central Government from time to time.

Fifthly, the Bank manages the clearing house operations for the banks at all important centres. Sixthly, it also performs important advisory functions such as giving advice to the diffeient governments and banks on financial and banking affairs. It acts as an agency for the collection and publication of official statistics and information.

Lastly, it may also accept deposits from any person or institution without interest, purchase and sell gold or government securities, to borrow money from a scheduled bank in India or a central bank of any other country for a period not exceeding 30 days, or to open accounts with or make agency agreements with central banks in other countries etc.

Reserve Bank's control over the money market : Before the passing of the Banking Regulation Act, the Reserve Bank of India possessed mainly two weapons to control the operations of the money market,—*viz.*, its power to lend at the Bank rate or rediscount eligible bills of exchange, and its power to engage in open market operations.

The Bank has been functioning since 1935. During these 31 years, there have been only seven changes in its Bank rate. At the time of its inception it started with a Bank rate of 3½ p.c. The rate was lowered in November 1935 to 3 p.c. This rate remained in force for 16 years, when it was again raised to 3½ p.c., in November, 1951 at which level it has remained till May, 1957 when it was raised to 4 p.c. It has since been raised to 4·5 p.c. in 1962. It was later raised to 5 p.c.

and further to 6 p.c. Movements of the Bank rate have usually been followed by similar movements in all other money rates in the organised sector of the money market. In the organised sector the Bank rate has proved to be an effective instrument for the control of the money market.

It is of course true that a small rise in the Bank rate cannot effectively check the rate of creation of credit. It will not prove deterrant enough in the face of an inflationary situation. But a rise in the Bank rate gives a sudden jolt to the money market and serves as a danger signal or an outward expression of the Reserve Bank's determination to cry a halt to the rate of creation of credit. Its psychological effects were, therefore, decisive. Moreover, banks have now-a-days fallen into the habit of borrowing from the Reserve Bank, especially during the busy season. A change in the Bank rate is likely to be passed on by the banks to their customers, and will influence their attitude towards the grant of new loans and advances. On the whole, the Bank rate is coming to assume a position of some importance in the money market, at least during normal seasons.

The Reserve Bank has also full authority to engage in open market operations, *i.e.*, sale or purchase of government securities in the market for the purpose of achieving certain objectives. It has engaged in such operations from a long time for the purpose of maintaining the prices of securities at reasonable levels, and also for neutralising as far as possible the impact of changes in the balance of payments upon the money market. During the war and post-war period it adopted the practice of buying government securities directly from the scheduled banks at the beginning of the busy season and selling them back to the banks with the onset of the slack season. In this way it supplied funds directly to the banks and withdrew them when necessary without disturbing the security market. In November, 1951, when the Bank rate was raised, it announced its decision to give up such a practice of buying government securities directly from the banks. This change in the open market operations had the immediate effect of putting pressure on the banks to slow down the rate of creation of credit during the busy season. Open market operations have not been carried out for purposes of monetary control. The Reserve Bank is also authorised to adopt the method of variable reserve ratios. It may raise the reserve ratio from 3 p.c. to 15 p.c. It can also raise the reserve ratio against new deposits upto even 100 p.c. if necessary. It had used this method only once in 1960.

The Banking Act of 1949 armed the Reserve Bank with extensive powers of control over the banking system as a whole. The Reserve Bank now possesses almost complete powers to control the operations of the banking system such as determining their lending policy, the types of paper they are to accept as a collateral and the rates of interest they can charge. It can prevent banks or a particular bank from making certain types of investments. It has been operating the selective credit control measures to regulate bank advances against foodgrains and certain other commodities under the provisions of this Act.

In one respect the Bank's control over an important sector of the money market is incomplete. It has not yet been able to establish any direct link with the indigenous bankers who constitute an important part of the Indian money market. Several schemes to that effect have been put forward from time to time, but none has yet been carried through. Its influence over this sector of the money market is thus mainly indirect, and to that extent hampers its control over the operations of the money market.

The Reserve Bank (Amendment) Act of 1956 : This Act was passed in September, 1956 to enlarge the powers of the Reserve Bank so as to enable it to control the operations of the banks more effectively than before. Financing of the Second Plan involved large-scale creation of paper currency notes. The government will have to take recourse to deficit-financing as a result of which the note issue will expand considerably. Such an increase in the amount of note issue is likely to lead to large-scale creation of bank credit. As these additional paper currency notes are deposited at the banks, it would increase the reserves of the banking system. As their reserves rise, banks may create large amounts of bank credit. If this happens, the danger of inflation will increase. So to prevent the occurrence of such inflation, the Act has sought to provide additional powers to the Reserve Bank. The provisions of this Act relating to the note issue have already been discussed in Chapter 34.

The amending Act enables the Reserve Bank to vary the rserves ratios of the scheduled banks within certain limits. Under the previous Act, the scheduled banks had to keep at the Reserve Bank balances equal to at least 5 p.c. of their demand deposit and 2 p.c. of their time deposits. These ratios may now be raised by the Reserve Bank to 20 p.c. in the case of demand deposits and 8 p.c. in respect of time deposits. Further,

the Reserve Bank may require scheduled banks to maintain with it additional cash reserves in relation to the excess of demand and time deposits over their level on a particular date, subject to the condition that the overall cash reserve ratios do not exceed 20 p.c. and 8 p.c. respectively. For example, a particular bank has Rs. 100 crores of demand deposits on a date and Rs. 20 crores of time deposits. After three months, its demand deposits increase by Rs. 10 crores and time deposits by Rs. 3 crores. The Reserve Bank may require this bank to maintain a reserve equal to, (say), 30 p.c. of its additional demand deposits over the level of the original date, and 15 p.c. of its additional time deposits, the ratios in the case of the original deposits may not be raised.

Provision has also been made to enable the Reserve Bank to pay at its discretion, interest at rates to be determined, to the scheduled banks on the amount of reserves they are asked to maintain in excess of 5 p.c. of the demand deposits and 2 p.c. of the time deposits.

This Act has introduced the system of variable reserve ratios, which has been regarded as an important instrument of credit control. A large number of central banks, belonging to both developed and under-developed countries, have already been armed with this method of controlling the operations of the banking system. In countries like India, where the money market is comparatively under-developed, the orthodox methods of credit control (Bank rate and open market operations) are seldom fully effective. The system of variable reserve ratios is in several respects a more effective instrument than these orthodox weapons.

The amending Act has thus completed the process of equipping the Reserve Bank with the necessary instruments of control. It has, however, been urged by Dr. S. K. Basu of the Calcutta University that one defect of this Act has been its omission to arm the Reserve Bank with the power to apply the different methods of selective credit control. This criticism has some force, and in under-developed countries aspiring for a rapid rate of economic development it may be essential to control the flow of bank credit into particular channels. The Reserve Bank may control the lending operations of the banks under the Banking Act by asking them to control particular types of loans. Their power is now being used, for example, for the control of bank advances for speculative purposes in the share market, or against the speculative holding of foodgrains. But it may be desirable to authorise the Reserve Bank to

utilise the different types of selective credit control that have proved effective in other countries. Another amendment was made in 1962 under which a uniform ratio of 3 p.c. was prescribed for both demand and time deposits. The Reserve Bank was also authorised to raise this ratio to 15 p.c. for purposes of credit control.

The Reserve Bank and Indigenous Bankers : The role played by the indigenous banks in the Indian money market will be discussed later on. These bankers still follow the traditional methods of banking. They carry on their business on a hereditary basis with their own funds which are lent at comparatively high rates of interest. They also combine the business of banking with some other business or trade. For example, many of them engage in trade, move crops from the mandis to the ports and otherwise distribute goods and raw materials. They draw and discount hundis, the traditional bills of exchange. They play a major part in the supply of rural finance, and their role in the cities and towns is also highly important.

The Act setting up the Reserve Bank made no provision for establishing any direct link between these classes of bankers and the Reserve Bank. It only took cognisance of the commercial banks and the co-operative banks. After the Bank started working, its authorities have made several attempts to remedy this important defect in that Act. The first scheme that was circulated among indigenous bankers was considered by them as too stiff. So a second scheme was drawn up in the expectation that it would be more acceptable. According to this scheme, those indigenous banks whose paid-up capital amounted to Rs. 2 lakhs, and who were prepared to raise it to Rs. 5 lakhs within 5 years would be included in the schedule of the Reserve Bank. Such bankers would have to separate their non-banking business and confine themselves exclusively to banking proper. They must maintain proper accounts, prepare balance-sheets and submit them to the Reserve Bank. In return, they would be granted all privileges enjoyed by the scheduled banks, *i.e.* they would be entitled to borrow from, or rediscount bills, of exchange at the Reserve Bank on the same terms and conditions as in the case of the scheduled banks.

This scheme did not also find any favour with the indigenous bankers. They did not consider that the privilege of borrowing or rediscounting would provide enough compensation for the loss

of their non-banking business, or their observance of other conditions. Hence the scheme fell through.

At the present moment some indigenous bankers have been granted by the Reserve Bank the privilege of remittance facilities at concessional rates as has been granted to the scheduled banks.

The absence of any direct link between the Reserve Bank and the indigenous bankers who constitute a most important sector of the money market is a serious defect in the working of the monetary mechanism. The Shroff Committee (1954) has recently put forward a number of suggestions for enabling the shroffs to function more closely with the organised money market. It has recommended that steps should be taken to encourage the rediscounting of the usance bills of indigenous bankers by the Reserve Bank through the scheduled banks. It also hoped that the question of forging direct links between the Reserve Bank and the indigenous bankers should again be actively pursued.

Bank Rate Policy : When the Reserve Bank was set up in 1935, it fixed its Bank rate at 3½ p.c. This was subsequently lowered to 3 p.c. in 1935, at which level it remained till 1951. Thus there was no change in the Bank Rate for more than 16 years. In fact, in those early years, changes in the Bank Rate would not have mattered very much except as providing an indication to the money market as to the intentions of the Reserve Bank. Very few scheduled banks borrowed from the Reserve Bank in those days and so would not have been much affected by the change in the Bank Rate. This was, moreover, a period of cheap money policy, when changes in the interest rates would have been more in the downward direction than an increase.

So the first important change in the Bank Rate policy came in November, 1951, when the rate was raised to 3½ p.c. At that time the Indian economy was passing through a considerable inflationary rise in prices, accompanied by heavy deficit in the balance of payments. The banks had been lending very large sums to the market, the expansion in the total bank credit amounting to Rs. 186 crores in the busy season of 1950-51. This was a very large rate of expansion according to the then standard. The contraction in the volume of bank credit in the ensuing slack season was also below the expected average. So the Reserve Bank decided to adopt a restrictive monetary policy on the eve of the busy season of 1951-52. Not only was the Bank Rate raised by ½ p.c., but the Reserve Bank informed the banks that it would not buy government

securities from them at the beginning of the busy season, as was the previous practice. On the other hand, the banks would have to borrow the necessary funds from the Reserve Bank at the higher Bank Rate. This action was followed by an immediate increase in other rates of interest charged by the banks. Banks adopted a cautious lending policy and in the busy season of 1951-52, bank advances rose by only Rs. 62·36 crores. The total money supply with the public rose by only Rs. 8·40 crores during the busy season of 1951-52, as compared to Rs. 235·77 crores in the previous busy season. On the whole, therefore, this shift to a restrictive monetary policy proved to be successful. In order that this sudden change in monetary policy might not affect the flow of bank credit to the essential industries adversely, the Reserve Bank introduced the Bill Market Scheme under which banks were granted loans by the Reserve Bank at ½ p.c. below the Bank Rate against their demand promissory notes backed by approved usance bills of their customers.

The next change in the Bank Rate was made in May, 1957, when it was raised to 4 p.c. This was done to bring the Bank Rate into equilibrium with the rates at which loans were granted under the Bill Market Scheme. Such rates had been raised gradually to 4 p.c. from 3 p.c. mainly on account of the increase in the Stamp Duty on Bills. This rise in the Bank Rate did not have much influence on the money market, when scheduled bank advances continued to rise at progressively higher rates. The Reserve Bank felt that the time was not ripe for another increase in the Bank Rate which would raise the borrowing costs of the government. So it was decided in 1960 to restrict access to the Reserve Bank through other methods. It was decided to fix the quota of borrowing by each bank from the Reserve Bank, which was not to exceed 50 p.c. of the average reserves a bank was required to keep with the Reserve Bank during each week of the previous quarter. A bank would be allowed to borrow from the Reserve Bank an amount equal to this quota at the Bank Rate. If it wanted to borrow more than its quota, it would have to pay interest at 1 p.c. above the Bank Rate so long as the amount borrowed did not exceed 200 p.c. of its quota, and at 2 p.c. above the Bank Rate on amounts exceeding 200 p.c. of the quota. At the same time the banks were asked to raise their lending rates by ½ p.c., with a minimum of 5 p.c. and the interest on short-term deposits was not to exceed 2 p.c. This three-tiers system

was modified in July, 1962, when a bank was required to pay interest at the following rates :—4 p.c. up to 25 p.c. of the statutory reserve, 5 p.c. from 26 to 50 p.c. of the statutory reserve and 6 p.c. on the remaining 50 p.c. of the reserve. Any borrowing above this amount was to be on terms to be negotiated with the Reserve Bank. This three-tier system was later modified into two-tier from January, 1963, when a bank was allowed to borrow upto 50 p.c. of the statutory reserve at 4½ p.c., and 6 p.c. on the other 50 p.c. of the reserve. At the same time the Bank Rate was raised to 4½ p.c. in January, 1963, in view of the rise in the market rates of interest brought about by the Reserve Bank's credit restriction policy. The working of the three or two-tier systems was attended by credit stringency in the money market, leading to increases in the rates of interest. There were, of course, some restrictions on bank advances. But prices continued to rise.

The next change in the Bank Rate was made in September, 1964, when it was raised from 4½ p.c. to 5 p.c. At the same time a change was made in the system of borrowing. A bank could borrow unlimited amounts from the Reserve Bank at the Bank Rate so long as its "net liquidity ratio" was at or above 28 p.c. "Net liquidity ratio" was defined as the total of a bank's cash balances, balances with the Reserve Bank and other notified banks plus its balances in current account with other banks, plus investments in government securities minus its total borrowings from the Reserve Bank and the State Bank of India as a proportion of its demand and time liabilities. When its net liquidity ratio fell below 28 p.c., it had to pay interest at ½ p.c. above the Bank Rate on its entire borrowings for every 1 p.c. decline below the ratio. The Bank Rate was again raised to 6 p.c. in February, 1965 when the net liquidity ratio was raised to 30 p.c. So long as its ratio was at or above 30 p.c., it could borrow at the Bank Rate. But for every decline in the ratio by 1 p.c. or a fraction thereof, the rate of interest was to be raised by ½ p.c. above the Bank Rate.

The whole idea is not to restrict the volume of bank borrowing from the Reserve Bank, but to raise the cost of borrowing. Lest this might not lead to higher advances' rates, the Reserve Bank laid it down that the advances' rates were also to be raised up to the maximum of 9 p.c. These measures led to an all-round increase in money rates. But the busy season of 1964-65 closed with a record expansion in bank credit by Rs. 407 crores, banks borrowing in some cases even at 13 p.c.

from the Reserve Bank. In the face of rising prices and profits and the heavy demand for bank credit, rising interest rates did not prove to be an effective check against an increase in the volume of bank credit. Banks and their customers found it quite easy to pass on the burden of higher interest charges to the shoulders of the buyers in the shortage-dominated economy.

The Bill Market Scheme : In November, 1951, the Reserve Bank raised the Bank rate from 3 p.c. to 3½ p.c. At the same time it announced that in the coming busy season it would grant loans and advances to the scheduled bank at the new Bank rate against government securities, instead of buying government securities directly from the bank and selling them back to the later at the end of the busy season, as was the practice followed during the war. The intention was to make credit dearer in the market. As this might prevent the grant of loans by banks for legitimate purposes, the Reserve Bank evolved the Bill Market Scheme in January, 1952. Another reason for which it was introduced was to impart a certain measure of elasticity to the money market.

Under the Scheme, the Reserve Bank agreed to make advances to the scheduled banks in the form of demand loans against their promissory notes supported by usance bills or promissory notes of their customers. As banks normally grant loans, cash credit and overdrafts to their customers, they were permitted to convert a part of these borrowings into usance promissory notes for 90 days, and these could be lodged with the Reserve Bank as collateral for advances. In order to popularise the drawing of bills, the Reserve Bank agreed (*a*) to make advances against these bills at ½ p.c. below the Bank rate, and (*b*) to bear one-half of the cost of the stamp duty to be paid at the time of converting demand bills into time bills. The scheme was provisionally restricted to scheduled banks whose deposits were not less than Rs. 10 crores on December, 30, 1951. The minimum value of individual bills tendered was fixed at Rs. 1 lakh each, while a bank must take a minimum advance of Rs. 25 lakhs at a time.

The following table will show the total amount of advances granted by the Reserve Bank against bills during the years in which the Scheme has been in operation.

Borrowings of banks from the Reserve Bank

Year		Total borrowings from Reseve Bank	Borrowings under the Bill Market Scheme
Jan. 1952 to March,	..	Rs. 54·13 crores	Rs. 28·00 crores
1952-53	..	Rs. 164·00 ,,	Rs. 67·00 ,,
1953-54	..	Rs. 234·00 ,,	Rs. 97·00 ,,

In the year 1951-52, borrowings by banks from the Reserve Bank reached the maximum on March 14, when they amounted to Rs. 62·04 crores, of which borrowings against bills amounted to Rs. 19·64 crores, *i.e.*, 31·6 p.c. of the total. In the next busy season, that of 1952-53, the maximum bank borrowings amounted to Rs. 25·83 crores on May, 8, out of which borrowings under the Bill Market Scheme amounted to Rs. 15·24 crores, *i.e.*, 62·2 p.c. In the busy season of 1953-54, maximum bank borrowings were Rs. 33·91 crores on March 19, 1954, out of which borrowings under the Bill Market Scheme amounted to Rs. 15·24 crores, i.e., 62·2 p.c. In the busy season of 1953-54, maximum bank borrowings were Rs. 33·91 crores on March 19, 1954, out of which borrowings under the Bill Market Scheme amounted to Rs. 18·20 crores, *i.e.*, 53·3 p.c. of the whole. The Scheme has no doubt proved popular among the banks. It enabled the scheduled banks to borrow from the Reserve Bank for meeting their busy season demands without disturbance to their port-folio of government securities. Its popularity will be judged from the fact that during the first six months of 1954, the advances granted according to the Scheme amounted to Rs. 122·12 crores as against Rs. 60·84 crores during the corresponding period of 1953. Moreover, advances against government securities at Rs. 116 crores were smaller than the advances under the Scheme during these six months.

The Committee on Finance for the Private Sector (the Shroff Committee) recommended that the facilities available under the Scheme should be extended to scheduled banks having deposits of Rs. 1 crore, instead of Rs. 5 crores, which was the original provision, and that the minimum amount of each individual bill should be lowered to Rs. 50,000 instead of one lakh, and the minimum limit of advances to one bank at a time should also be lowered from Rs. 25 lakhs to Rs. 10 lakhs. The Reserve Bank has accepted these recommendations and the facilities of borrowing under the Scheme have been extended to all scheduled banks,

irrespective of the size of their deposits, and the minimum limits have been lowered as recommended.

It should, however, be frankly recognised that though the Scheme is called the Bill Market Scheme, it had not really set up a Bill Market. A bill market presupposes the existence of a number of dealers who are always prepared to buy and sell bills of exchange, and there should be active dealings in such bills. No such features are to be found in this scheme. All that has occurred is that banks induce their customers to convert a part of their cash credit or loans into bills which are then sold to the Reserve Bank of India at concessional rates. For the banks the scheme has provided a comparatively cheaper means of borrowing funds from the Reserve Bank. For the Reserve Bank it has provided an assurance that the funds it lends to Banks would be returned at the end of 3 months, when bills become mature and will be paid back. But whatever its other merit might be, the scheme has not led to the establishment of a Bill Market.

Selective credit control : As commodity prices began to rise from the level reached in the middle of 1955, there was a noticeable increase in speculative hoarding of foodgrains, and this was regarded as one of the factors responsible for the rise in prices. The Reserve Bank made use of general as well as selective credit control measures to cope with the situation. The Reserve Bank's lending rate under the Bill Market Scheme was raised from 3 p.c. to 3½ p.c. on November, 1956. But as the government raised the stamp duty on usance bills by half per cent, the effective borrowing rate of the scheduled banks actually rose to 4 p.c. from February, 1957. Simultaneously, the Reserve Bank also raised its lending rate on advances against government securities to 4 p.c.

Apart from these general measures, the Reserve Bank also took recourse to selective credit control measures. On May 17, 1957, it issued a Directive to banks asking them to refrain from excessive lending against commodities in general and not to grant fresh advances against paddy and rice to individuals in excess of Rs. 50,000 and to raise the existing margins against such advances by 10 p.c. They were also requested to bring down the level of advances against this commodity to a level not more than 125 p.c. of that in the corresponding period of the previous year. Later, such credit control measures were also extended to cover bank advances against wheat, gram and pulses, cotton

textiles, sugar etc. On June 1957, the margins were further raised by 5 p.c. (*i.e.* by 15 p.c. in all) so as to provide a margin of not less than 40 p.c. Further, banks were to maintain the total of such advances at levels not exceeding two-thirds in case of rice and paddy and three-fourths in the case of wheat and other foodgrains of the levels obtaining in the corresponding period of the previous year. These Directives were modified from time to time to suit the changing circumstances, and the Directives were modified in subsequent periods from regulation through margins to regulation of the aggregate level of advances against specific commodities.

In the initial stages the response to the new Directives was not fully satisfactory, and the Governor of the Reserve Bank issued letters to the defaulting banks. Later there was greater compliance. As regards the impact of these measures on the prices of these commodities there was more or less insignificant. But one must admit that the change in the prices of these commodities would depend primarily on the availability of their supplies relative to the rise in demand. Hence one must not rise to the conclusion that the selective credit control measures had proved to be ineffective. There is a good deal of truth in the contention of the Report on Currency and Finance (1958-59) that "the success of these controls is to be judged in a limited sphere, namely, their impact on the pressure of demand *originating from bank credit* ; in this sense the measures should be deemed successful ; but for their operation it is likely that the price situation might have been worse."

Other measures : In addition to these measures, the Reserve Bank also adopted other instruments for regulating the flow of bank credit. Thus during 1958-59, the Bank sold securities worth Rs. 90 crores to absorb some of the excess reserves of the banking system. Recourse was also had to what was known as moral suasion. The Governor of the Reserve Bank wrote letters to the banks and exercised his influence to induce them to bring down the total of advances to reasonable maxima.

Variable reserve ratios : The Reserve Bank received the power to vary the reserve ratios of the scheduled bank under the amending Act of 1956. This power was formally utilised for the first time on March 11, 1960, when the Reserve Bank asked the scheduled banks to maintain additional balances equal to 25 p.c. of the increase in their

total deposits since March 11. A further notification was issued on May 5, raising this percentage to 50. In addition, the Reserve Bank extended the selective credit control machinery to include bank advances against stock exchange transactions as well as unsecured loans. Banks were asked to maintain a minimum margin of 50 p.c. in respect of their advances against shares with regard to the additional deposit to be maintained with the Reserve Bank, the latter agreed to pay interest on such balances to the scheduled banks at the average rate of interest paid by them on their total deposits. It has subsequently decided to pay ½ p.c. more than the average deposit rates of the scheduled banks, subject to a maximum of 4½ p.c.

In addition, circular letters were issued asking them to reduce the total of bank advances by at least Rs. 100 crores during the slack season of 1959 and by at least Rs. 110 crores during the slack season of 1960. They were also asked to adopt a very cautious policy in the grant of advances against commodities not covered by the Reserve Bank's Directives.

These changes in monetary policy have been adopted against the background of the prevailing inflationary situation in the country. It appeared that the major inflationary factor was rather the high level of aggregate demand and this should be curtailed through monetary and other instruments of control.

Controlled expansion : The monetary policy which has been pursued by the Reserve Bank since 1956, the first year of the Second Plan, has been regarded as one of 'controlled expansion'. The country is pursuing a policy of economic expansion with a large amount of investment expenditure in various projects, agricultural and industrial. Such a policy of economic development which involves increasing output naturally call for some expansion in bank credit and money supply for financing such increases in investment. At the same time, the population of the country is increasing at the rate of more than 2 p.c. per annum. This also requires some expansion in money supply. On the other hand, a part of the new investment has a comparatively long gestation period, and so the final output may not be available at once. Moreover, a considerable part of the new public investment expenditure is being financed by recourse to the printing press and to the banking system. These have serious inflationary consequences for which it will be necessary to exercise suitable restraints on the rate of creation of bank

credit and money supply. So while some expansion in money supply is necessary every year, the expansion has to be controlled properly to prevent the emergence of inflationary pressures in the economy. This is the *rationale* behind the policy of controlled expansion as it has been carried out by the Reserve Bank of India.

This policy has been followed in several directions. Thus while no restrictions have actually been placed on borrowing from the Reserve Bank by the scheduled banks, the latter had been required to pay increasingly higher rates of interest on such borrowing. The control was thus sought to be exercised through the banks' unwillingness to pay higher rates of interest. This was combined with the vigorous application of selective credit control measures, under which the Reserve Bank made a serious attempt to regulate and restrain the flow of bank credit to undesirable channels like the foodgrains market, or the market for certain scarce commodities like sugar or raw cotton etc., and for speculative purposes. Banks were continuously reminded to avoid granting such loans, and to accept requests for banking accommodation for productive purposes only. From time to time, certain concessions in the shape of larger credit facilities were granted to particular industries under difficult circumstances to enable them to tide over such difficulties, for example, to the tea industry, or to the sugar industry or to the cotton textile industry. Some expansion in bank credit was tolerated and even encouraged on these occasions in an otherwise credit restriction phase. On the whole attempts were made to deal with particular situations deftly and quickly to ensure that nobody suffers really from a dearth of bank credit unless absolutely necessary.

One evidence of the flexibility of this policy has been provided by the recent announcement regarding the *"Selective liberalisation of credit"*, made by the Reserve Bank in November, 1965. Under this change in policy, requests from banks for increased credit facilities to finance the industries connected with defence production, exports and the procurement of foodgrains were favourably treated, while credit was to be tightened in many other sectors, mostly non-priority sectors. Thus the policy has two faces,—expansion to be allowed in a number of sectors considered to be of vital importance, and restriction in most other sectors, and both these flows—of expansion and restriction were to be regulated deliberately against the background of the general economic conditions of the country.

It is difficult to say how far this policy succeeded in its objectives. Inflationary rise in prices has continued unabated in spite of the adoption of this policy. The expansion in bank credit and money supply has also proceeded more or less unhampered. In fact, the rate of interest is a rather poor instrument for restraining the demand for bank credit against the background of inflationary conditions, and a real check to expansion can only come with the regulation of the availability of central bank credit. That has never been attempted on Reserve Bank's own admission. So the accent of this policy has been more on expansion and less on control.

The Reserve Bank and non-banking companies : The acceptance of deposits by some of the industrial companies has always been a feature of the Indian money market. The textile mills of Ahmedabad, for example, accepted deposits from the public and used these deposits to finance their requirements. Of late non-availability of bank advances due to the policy of credit restriction had led a large number of non-banking companies to compete for deposits from the public, and as this practice threatened to become almost general, the government passed suitable legislation in 1963 to enable the Reserve Bank to exercise control over this particular phenomenon. This act authorised the Reserve Bank to regulate or even prohibit the issue of prospectus or advertisement by such companies soliciting deposits from the public, to call for returns and information as to their deposits, the rates of interest and the maturity of such deposits. The Reserve Bank may prohibit any such company which does not comply with its directions from accespting deposits. It may also call for from the financial institutions information relating to their paid-up capital, reserves or other liabilities, investments, terms and conditions of advances etc. and to give directions to them regarding the conduct of their business.

Action had already been taken under this act, and all such companies including financial institutions had been acquired to provide necessary information to the Reserve Bank. A survey of the data thus obtained showed that a large proportion of such deposits accepted by these companies were withdrawable on demand or on the expiry of a specified period, generally small. So the Reserve Bank issued a directive to these companies and financial institutions asking them not to accept deposits repayable on demand or notice. The non-financial companies

were further prohibited from accepting deposits repayable in less than 12 months ; the financial institutions *e.g.*, the hire-purchase companies were, however, allowed to accept deposits withdrawable after 6 months. The directives also require all such companies to disclose certain particulars in their advertisements seeking deposits, to furnish receipts to depositors, to maintain proper registers of all deposits received by them and to include certain information relating to deposits in the reports of the Board of Directors to be laid before the general meeting. The hire-purchase companies were further required to maintain in India liquid assets in the form of cash or Post-office Savings Bank deposits or in current account with scheduled bank or in unencumbered trustee securities a sum equal to 9 p.c. of their assets in India, and to secure that the amount of instalment receipts under hire-purchase contracts during each half year is not less than 25 p.c., of the outstanding amount as at the close of the previous accounting year. These two directives were subsequently amended in April, 1966, requiring among other things such companies to furnish to the Reserve Bank audited balance sheets and interim accounts so long as they hold deposits. In order to study these data and to look after the enforcement of these directives, the Reserve Bank has established a Department of Non-Banking Companies at Calcutta in March, 1966.

This is a step in the right direction, and though the total of such deposits received by these companies is as yet not so large in comparison with the resources of the banking system, it is highly desirable that the monetary authorities should keep themselves informed of the growth of this practice and to adopt suitable measures of regulation as and when necessary.

Questions

1. Describe the constitution and functions of the Reserve Bank of India. Show how it will control credit.

2. "The principal tasks of the Reserve Bank are to control the credit situation." Discuss.

Describe the principal instruments of credit control at the disposal of the Reserve Bank of India (C. U. B. Com. 1961).

3. Describe the relation of the Reserve Bank with the central and state governments. Is it desirable to increase the control of the government over the Reserve Bank ?

4. Examine the nature of the control which the Reserve Bank maintains over the scheduled banks. What are the advantages of the control ? (C. U. B. Com. 1957).

5. What are the main services which the Reserve Bank performs for the Indian money market ?

6. Write a short note on the credit policy of the R. B. I. with particular reference to the control of inflation. (C. U. B. Com. 1960).

7. Describe the various measures adopted by the Reserve Bank of India for controlling the credit situation during the Plan period. (C. U. 1961).

CHAPTER 36 OTHER CONSTITUENTS OF THE MONEY MARKET

A money market is a market for the lending and borrowing of money. The main lenders in the market are the joint-stock banks including the State Bank of India and the exchange banks, the co-operative banks including the land mortgage banks, the Industrial Finance Corporation and similar other institutions, the insurance companies and the indigenous bankers. Over all these lenders there is the Reserve Bank of India whose duty it is to guide, inspire and control the operations of these lenders. It is usual to state that the Indian money market consists of two parts,—the organised and the unorganised sector. The unorganised sector is constituted by the indigenous bankers who pursue the banking business on traditional lines. The rest are part of the organised sector—they pursue the lending business on modern lines.

We have already discussed the functions and working of the co-operative banks, the Industrial Finance Corporation and similar other corporations, and the Reserve Bank of India in earlier chapters. It remains now to examine the part played by the commercial banks and the indigenous bankers.

Joint-stock banks : Joint-stock banks which pursue ordinary commercial banking business have been classified into two groups—the scheduled banks and the non-scheduled banks. Banks whose paid-up capital and reserves amount to at least Rs. 5 lakhs have the right to be included in the schedule to the Reserve Bank of India Act. These are known as the "scheduled banks." Those whose paid-up capital and reserves are less than Rs. 5 lakhs fall in the group, "non-scheduled banks." There were 76 scheduled banks and 33 non-scheduled banks as on March, 1966. It should be noted that the scheduled banks include all the largest banks, *viz.,* the State Bank of India, the Exchange Banks and other large Indian banks. Though these banks constitute 69 p.c. of the total number of banks in India, their aggregate paid-up capital and reserves amounted to Rs. 83·30 crores, whereas those of the 33 non-scheduled banks amounted to only Rs. 1·95 crores. Out of a total deposit of Rs. 2973·84 crores held by all banks in March 1966, scheduled banks held Rs. 2949·93 crores, *i.e.,* about 99.2 p.c. of the total. The average deposit of a scheduled bank amounted to Rs. 38·8 crores as against an average of only 7·2 lakhs in the case of a non-scheduled bank.

The business of the scheduled banks is best studied under three broad headings, *viz.,* the functions of the State Bank of India, those of the other Indian banks, and lastly, those of the foreign exchange banks. We propose to study these three groups separately.

The State Bank of India : Though an ordinary commercial bank, the State Bank of India occupies a special position in the Indian money market. In the first place, unlike other Indian banks, its constitution and functions are governed by a separate Act of the legislature. The other Indian banks are organised under the Indian Companies Act. Secondly, from its very inception, this Bank has been associated with the government. Until the formation of the Reserve Bank, it held all the deposits of the government, and performed some of the central banking functions. The central government nominates a number of Directors on the Board of Directors of the Bank, whereas this is not the case with other banks. Thridly, it acts as the agent of the Reserve Bank of India in places where the latter has no branch. This gives it added prestige. Lastly, it is the largest commercial bank in India. Its total deposits amounted to about Rs. 230 crores, *i.e.,* more than 26 p.c. of the deposits of all scheduled banks. Other banks are in the habit of borrowing from the State Bank whenever there is a need of cash balances.

The former name of the State Bank of India is the Imperial Bank. It was established in 1921 by amalgamating three Presidency Banks,—the Banks of Bengal, Madras and Bombay. An Act was passed by the Indian Legislative Assembly to facilitate this amalgamation. This Act, as subsequently amended, governed the constitution and functions of the Bank. This Bank was appointed as the banker to the government. It kept the balances of all governments, central and state, free of interest and managed the public debts. In return, certain restrictions were placed on its activities. It could not, for example, lend for more than six months, or against the security of any immovable property or of its own shares. It could not also engage in foreign exchange business. Besides these restrictions, the government had the right to nominate two Directors to the Central Board of Directorate of the Bank, and to nominate the Controller of Currency as an *ex-officio* Director without any power to vote.

With the establishment of the Reserve Bank, it lost all its functions as the banker to the government. The Reserve Bank became the holder of all government balances and took over the functions of the management of

the public debt and of the clearing houses. In return for the loss of these functions, some of the restrictions placed on its functions were withdrawn from 1935. For example, it was allowed to engage in foreign exchange business. It was also appointed as the agent of the Reserve Bank of India in places where the latter had no branches.

The former Imperial Bank of India held a commanding position in the money market. Its call loan rates served as the barometer of the short-term money market. Other banks were in the practice of borrowing from it as they did from the Reserve Bank. In fact, in the slack season of 1953, borrowings of scheduled banks from the Imperial Bank invariably exceeded their borrowings from the Reserve Bank.

Nationalisation of the Imperial bank. The Imperial Bank frequently came in for criticism. For example, it was urged that the bank discriminated in favour of European firms against Indian concerns, and that it had not provided adequate facilities for the recruitment and training of Indians for the higher posts. Hence there was a demand in the country for the nationalisation of this Bank, and in February, 1948, the Finance Minister announced in the Parliament that the government had accepted the policy of nationalising the Bank.

In 1954, the Report of the Committee on Rural Credit Survey, set up by the Reserve Bank of India, recommended the conversion of the Imperial Bank into the State Bank of India. In accordance with this recommendation, the government passed an Act for nationalising the Imperial Bank. The shares of that Bank were acquired by the Reserve Bank on behalf of the government, and the State Bank of India began to function from July 1, 1955.

Among the immediate objectives of the State Bank of India is a vigorous drive to expand the number of branches, especially in the rural areas. The Act laid down that the Bank was to establish at least 400 new branches over a period of 5 years. As a measure of compensation for the initial losses on unremunerative branches, provision was made for a special Integration and Development Fund, where the dividends payable to the Reserve Bank on its shares would be credited. This Fund was to be utilised for meeting the initial loss on the opening of unremunerative branches. Another function of the State Bank of India was the provision of cheap remittance facilities. Time alone will show

how far these functions will be discharged to the desired extent by the State Bank of India. By 1960, the State Bank had completed its task of establishing 400 new branches.

Other Indian joint-stock Banks : Commercial banking on modern methods began in India with the Agency Houses, established by the former servants of the East India Company. These Agency Houses combined their banking business with some other trading functions. The first joint-stock bank, the Bank of Hindusthan, was established at Calcutta under European management. This Bank had to close its doors in the crisis of 1829-37. The first purely Indian joint-stock bank was the Oudh Commercial Bank, which was started in 1881. It was followed by the Punjab National Bank in 1894 and the People's Bank of India in 1901. The Swadeshi movement of 1905 gave a great stimulus to the establishment of Indian banks, and a number of such banks were started. There was, however, a serious banking crisis in 1913 when several banks closed their doors, following the failure of the People's Bank of India, one of the largest Indian banks. There was, again, another banking crisis in the period of the post-war depression in 1921-22, heralded by the failure of the Alliance Bank of Simla, an important bank under European management. The growth of Indian joint-stock banking since 1920 is exhibited in the following table.

TABLE 1

Indian Joint-Stock Banks, 1920-1966

Year	No. of Banks	Deposits
1920	61	Rs. 159·77 crores
1925	75	„ 141·21 „
1930	89	„ 151·62 „
1935	101	„ 168·81 „
1940	298	„ 223·74 „
1945	468	„ 908·86 „
1950	460	„ 826·40 „
1955	475	„ 783·57 „
1960	342	„ 1658·77 „
1966	109	„ 2909·68 „

Functions : These banks perform the usual commercial banking functions like the acceptance of deposits of various kinds, granting loans and advances, cash credits and overdrafts, discounting hundis and bills of exchange etc. They grant loans and advances against gold or government securities and other stock exchange securities etc. They supply short-term credits to industrial concerns on the security to their stock-in-trade. Recently a number of them have begun to undertake foreign exchange business and have started branches in foreign centres for this purpose. In spite of this welcome advance, the part played by Indian banks in the financing of foreign trade of the country is still insignificant. The exchange banks occupy a dominant position in this respect.

Structure of assets and liabilities : In this section we shall study the structure of the assets and liabilities of the scheduled and non-scheduled banks in the year 1960-61.

At the end of 1960-61 the paid-up capital and reserves of the Indian scheduled banks stood at Rs. 68·76 crores, while those of the non-scheduled banks at Rs. 6·89 crores. The capital and reserves structure varies considerably with different groups of banks. Thus 28 large Indian scheduled banks had between them Rs. 58·9 crores of capital and reserves, while the remaining 30 Indian scheduled banks held capital and reserves of only Rs. 8·6 crores. Among non-scheduled banks concentration of capital and reserve is even more marked, 40 non-scheduled banks had capital and reserves amounting to Rs. 4·1 crores, while the remaining 229 banks had capital and reserves of only Rs. 3·8 crores. The ratio of paid-up capital and reserves of only Rs. 3·8 crores. The ratio of paid-up capital and reserves to deposits in the case of the Indian banks compare favourably with those of British or American banks ; the ratio being 10 p.c. in Indian banks against 8 p.c. in American banks and 3 p.c. in British banks.

The same concentration was to be found in the case of deposits. Only 6 p.c. of the Indian banks had each capital and reserves of Rs. 50 lakhs and more, but they accounted for over 75 p.c. of total capital and reserves and about 87 p.c. of the total deposits. At the other end 72 p.c. of the Indian banks accounted for 7 p.c. of the total capital and reserves and only 3 p.c. of the total deposits.

Banks now work with lower cash ratios, the average for scheduled banks being 6·2 p.c. in 1962-63 as against 10 p.c. in 1939 and 14·6 p.c.

in 1949. The average cash ratio of non-scheduled banks is a little higher, being 7·3 p.c. 1962-63. Investments in government securities formed 35·9 p.c. of the deposits in the case of the scheduled banks and 33·1 p.c. in the case of non-scheduled banks. Loans and advances were, on average, 60·6 p.c. of the deposits in the case of scheduled banks and 63·1 p.c. in the case of non-scheduled banks.

Branch-banking : With regard to branch-banking, the Indian banking system stands midway between the British and the American banking systems. In Great Britain, branch-banking is prevalent extensively, the "big five" dominating the entire banking system with a very large number of branches. At the other extreme stands the American banking system, where, though the large banks have branches, the vast majority are unit-banks with virtually no or small number of branches.

In India, 276 banks had 5261 branches in 1962. Of these, the State Bank of India had 1002 branches, and the Exchange Banks 81 branches. Excluding these from the total, the Indian scheduled and non-scheduled banks, numbering 253 banks, had 4178 branches, 196 non-scheduled banks had only 657 branches, an average of about 3 branches including the head office. The 57 Indian scheduled banks had 3521 offices, *i.e.*, an average of about 61 offices.

During the last war there was an indiscriminate increase in the number of branches, most of which were unremunerative. In order that the competitive opening of branches may not lead to the weakening of banks, the Banking Companies (Restriction of Branches) Act of 1947 and the Banking Companies Act of 1949 have sought to restrict the power of banks to open branches. Branches cannot, in future, be opened by a bank without permission from the Reserve Bank of India. This resulted in the decline in the number of branches, which was also brought about by the amalgamation of banks and the closing down of uneconomic branches. Thus the number of offices of banks declined from 4674 in 1948 to 4353 in 1950 and to 4036 in 1953. This is not an unhealthy development. The decrease in the number of branches is concentrated mostly in the case of the non-scheduled banks, compensated to some extent by an increase in the number of branches opened by scheduled banks. Thus in 1953 the scheduled banks opened 90 branches (including 30 by the State Bank of India), while 77 branches of non-scheduled banks were closed down.

Branch-banking is certainly a desirable development provided that it proceeds in a balanced manner, thereby increasing the strength of the system. Time has come for the bigger banks to be more enterprising and to adopt well-planned schemes for opening new branches, especially in the main rural centres. At the present moment banks claim that the chief hindrance to the opening of new branches is the high operating costs resulting from the various Bank Awards. As banks have to pay salaries fixed according to the scales laid down in the Awards even in new branches it would prove uneconomical. The new branches could not meet their expenses within the first few years. The authorities should draw up a scheme under which banks opening branches in selected places would be paid some subsidy to enable them to meet the high cost involved.

The joint stock banks and the Reserve Bank of India: For purposes of discussing the relationship between the joint-stock banks and the Reserve Bank, the former are to be divided into two broad groups,—the scheduled and non-scheduled banks. All banks with a paid-up capital and reserves of Rs. 5 lakhs or more are entitled to be included in the first schedule of the Reserve Bank Act. They are known as the scheduled banks and numbered 94 in 1959. The rest, (*i.e.*, those whose paid-up capital and reserves are less than Rs. 5 lakhs) are known as the non-scheduled banks and their number had declined to 33 in 1966. We shall, first of all, discuss the Reserve Bank's relationship with all banks in general, and examine the case of these two types of banks separately.

The Reserve Bank's relations with banks in general are governed by the provisions of the Banking Act of 1949. Under that Act, no bank can carry on its business unless it has got a licence from the Reserve Bank. It cannot open a new branch without the permission of the Reserve Bank. It must submit weekly and monthly statements of its accounts to the Reserve Bank which may require it to furnish the latter with all other information. The Reserve Bank may also give directions to all banks or to any bank as to the purposes for which advances may or may not be made, the margins to be kept in respect of secured advances and the rates of interest to be charged on advances. It may also caution or prohibit banks or any bank against entering into any particular transactions, and may inspect the books and accounts of any bank.

These are the general powers of control and regulation which have been granted to the Reserve Bank which has other relationship with the scheduled banks. This relationship is governed by the provisions of the Reserve Bank Act. Under that Act, the scheduled banks have to keep balances with the Reserve Bank equal to three per cent of their demand and time deposits. This ratio can be raised to 15. In return, the scheduled banks have been granted the privilege of borrowing from, or rediscounting at the Reserve Bank against bullion or trustee securities or eligible bills of exchange or promissory notes etc. They can also borrow from the Reserve Bank under the Bill Market Scheme. They also enjoy the privilege of remittance of funds through the Reserve Bank at concessional rates.

The recent Banking Companies (Amendment) Act of 1956 has further strengthened the control of the Reserve Bank over the joint-stock banks. Under this Act, the appointment of the managing director or wholetime director or the manager or the chief executive officer of a bank is subject to the previous approval of the Reserve Bank. The Reserve Bank can also prohibit the payment of remuneration to the top officials of banks which it considers to be excessive. It can also appoint observers for watching and reporting on the conduct of affairs of a bank. Every bank will also have to make such changes in its management as the Reserve Bank may consider necessary. The Reserve Bank may also issue directives to a bank in relation to matters of policy or administration in the national interest or in the interest of the institutions themselves. Under an amendment made in 1962, banks would now have to keep at least 25 p.c. of its total deposits invested in cash or gold or unencumbered approved securities valued at the current market price. This provision has come into effect from September, 1964.

The non-scheduled banks, the central co-operative banks and certain co-operative credit banks have to maintain by way of cash reserves in cash with itself or in balances with the Reserve Bank a sum equal to three per cent of their demand and time deposits. A number of them also enjoy the privilege of remittance of funds at concessional rates.

Exchange banks : These are foreign banks or branches of such banks, and are so called because their main business is to deal in foreign exchange. There are 14 such banks in 1965, of these two deal mainly with tourist traffic. Three have considerable business in India, while the rest are branches of large banks operating throughout the East.

Functions. Like ordinary commercial banks these banks also undertake all kinds of banking business, such as the acceptance of deposits, the grant of loans and advances etc. But they have specialised in financing the foreign trade of the country. They purchase or discount export and import bills of exchange. While this still remains their special line of business, they are also taking an increasing part in the internal banking business. Thus these 14 banks had 81 offices in 1962. Their total deposits amounted to Rs. 267·25 crores in the same year as compared to Rs. 155·4 crores in 1949. They are now taking an increasing part in financing the internal trade of the country. Thus the exchange banks finance a large portion of the jute trade in West Bengal, leather trade in Kanpur, cloth trade in Delhi etc.

Methods of financing foreign trade. As regards the method adopted to finance exports, Indian exporters draw up bills of exchange against credits opened by the foreign buyers with foreign banks. These bills are D.A. bills (documents against acceptance) with a maturity of 3 months. These bills are sent by the exchange banks to the foreign countries and after acceptance are discounted in the London discount market. As the shipping documents are handed over to the buyers after acceptance of the bills, the latter could get possession of the goods after the arrival of the ships. Imports are usually financed by means o D.P. bills (documents against payment) of exchange drawn on Indian importers. The exchange banks present these bills to the importers and the attached documents are delivered only after the latter execut trust deeds in favour of the banks, under which the ownership over th goods remains with the banks until payment is over. Importers hav to pay interest at 6 p.c. upto the period when the proceeds of the bill reach London. In other words, Indian importers have to pay interes on funds obtained from exchange banks at considerably higher rates.

When India has a favourable balance of payments, export bill exceed import bills in value and the purchase of export bills mean that the funds of the exchange banks are transferred to London. Thes funds are brought back to India by the exchange banks who sell sterlin to the Reserve Bank, when necessary, or import precious metals for sal in India. Previously exchange banks brought large amounts of fund from the London money market to finance their busy season require-ments. But now-a-days they are coming to rely on the resources o

the Indian market for this purpose, and borrow heavily from the market during the busy season.

The exchange banks and the Reserve Bank. As the paid-up capital and reserves of these exchange banks are comparatively large, they are all included in the first schedule of the Reserve Bank, and so enjoy all the privileges and obligations of scheduled banks. They have to maintain balances with the Reserve Bank equal to 3 p.c. of their demand and time deposits. They have to submit statements of their accounts in respect of their Indian business regularly to the Reserve Bank. In return, they enjoy all the usual borrowing and rediscounting facilities granted by the Reserve Bank to scheduled banks. They have all been granted licence as "authorised dealers" by the Reserve Bank and so can buy and sell foreign currencies.

Before 1949, there were no other restrictions on their activities beyond those stated above. The Banking Companies Act of 1949 contained a number of provisions specially applicable to foreign banks. These banks are now required to take a licence from the Reserve Bank. They have to keep in India at least 75 p.c. of their demand and time deposits in such assets as eligible bills or promissory notes, export and import bills drawn on and payable in India etc. They must keep in deposit with the Reserve Bank an amount equal to at least Rs. 15 lakhs, if the bank has an office in Calcutta or Bombay Rs. 20 lakhs either in cash or in approved securities or in both. If any of these banks closes its business in India, such deposits shall be an asset on which the claim of the creditors of the company shall be a first charge. Lastly, the operations of these banks would be subject to the control of the Reserve Bank, equally like any other bank, in respect of advances, etc. There is no doubt that the Reserve Bank has full powers to control the activities of these banks in respect of their Indian business. It can control their foreign exchange transactions under the Exchange Control Regulations and their internal lending operation under the Banking Companies Act.

Comments on the position of exchange banks. These banks are foreign banks and they occupy a dominant position in the financing of the foreign trade of the country. Of late, they have begun to compete in securing internal business. Naturally they have come in for a good deal of criticism. It is certainly a matter of serious concern that the share of Indians in the financing of foreign trade of the country

should be so small. As a result, we have to pay large sums as commission, brokerage and insurance premia to foreign concerns. In recent times some of the Indian banks have become more enterprising and have opened a number of branches in foreign centres with the purpose of securing a share in the financing of the foreign trade. The Indian banks had in 1962, 103 branches outside India including branches in Pakistan and French India. Of these 6 were in the United Kingdom, seven in Burma, 15 in East Africa, 2 in Japan etc. From statements published by the Reserve Bank, it appears that the share of Indian banks in the financing of foreign bills has increased from 19 p.c. of the total in 1950 to 23 p.c. in 1953 and to 23 p.c. in the first months of 1954. This is a welcome trend.

The other charges against the exchange banks are that (*a*) they prefer their own nationals and have not trained up Indians for the higher posts ; (*b*) they force the Indian exporters to insure their goods with foreign insurance companies and in this way discriminate against Indian companies, and (*c*) in the matter of granting loans and advances they give preference to their own nationals as against Indians. These charges have, of course, been denied by the exchange banks and it is difficult to verify them. The remedy lies in greater participation of Indian banks in the conduct of foreign exchange business, with the active co-operation and help of the Reserve Bank and the Government of India. If individually Indian banks find it difficult to secure enough business in this direction, they might join together in a consortium and set up an Indian Exchange Bank by taking up shares in it. Such a bank may be in a position to compete with the exchange banks and secure some of the business of financing foreign trade.

A Note on the methods of financing trade. The Reserve Bank of India has published a note dealing with the method of financing foreign trade. It has collected statistics from the year 1950. It was found that while an appreciable part of India's exports, *i.e.* 67 p.c., was financed through the drawing of export bills, only about one-fourth of the total imports were financed through bills. The reasons of financing of a small portion of the import trade through bills lay in the fact that a considerable part of our imports consisted of machinery for which the drawing of bills was obviously not suitable. Moreover, fairly large imports, such as those of petroleum were paid for only when the goods were actually sold. So in their case no bills were drawn to finance their

purchase. Another reason might be that banks sold or discounted import bills in foreign countries without bringing them to India, and so these have not been included in the statistics collected by the Reserve Bank.

Among the bills which were drawn up, sterling bills still predominated, forming 65 p.c. of the total. Bills drawn in terms of U.S. dollar and the Indian rupee formed about 20 p.c. and 14 p.c. respectively of the total.

Indigenous bankers : The system of banking existed in India from very ancient times. Banking was then organised in the form of personal or family businesses, and bankers known as the "shrestis" commanded a high position in society. They accepted deposits, acted as money-changers and financed the internal trade and the collection of the revenues of the government through the issue of *hundis* or internal bills of exchange. This form of business has continued even up to the present day, and the persons who pursue this type of banking business on traditional lines are collectively known as the indigenous bankers. They are called by various names in different parts of the country such as shroffs, seths, sahukars and others. They form an important part of the Indian money market. Their importance will be obvious from the fact that India possesses 3018 towns and 558089 villages, while the total number of banking offices amounted to 5160 in 1962. When we consider that the majority of banking offices are to be found mainly in the larger towns, it is obvious that almost the whole of the village areas and a large number of towns have no banking office. They are served mostly by the indigenous bankers.

The banks can be grouped into three classes :—(*a*) those whose principal business is banking, (*b*) those who combine their banking business with some other trading function or functions, and (*c*) those who are principally traders, but employ surplus funds in banking. The majority of indigenous bankers belong to the second class.

These banking institutions vary in their size from petty money-lenders to substantial shroffs who carry on a large and specialised business which at times exceeds that of some of the scheduled banks. Those who undertake this type of business usually belong to certain castes or communities such as the Multanis, Marwaris, Natukottai Chettis or the Kalladkurchi Brahmins.

The *Multanis* had their headquarters formerly at Shikarpur. But now they have spread all over India, and pursue their business mainly in cities and towns. They usually restrict themselves to their banking business and deal in hundis, and whenever necessary, borrow from the joint-stock banks. The latter maintain an approved list of such bankers and fix up their credit limits. The *Marwaris* are primarily merchant bankers. They do hundi business, lend money and deal as a merchant. They lend against goods supported by a demand promissory note or even against a mortgage of landed property. They prefer to rely on their own funds, but accept deposits and borrow from banks during busy seasons. The *chettiars* used to accept deposits and granted loans on the basis of hundis and on the pledge on hypothecation of goods or against personal security. The *kalladkurchi Brahmins* also accept both fixed and current account deposits.

Their business is usually a family concern, and they operate with their own funds. They do not, as a rule, try to attract deposits from the public like the joint-stock banks. But some of them accept deposits from their friends and relations. Secondly, they grant loans against all kinds of security such as gold or jewellery, land, promissory notes, *hundis* etc. They lend against the personal credit of the borrowers to a much greater extent than is done by the joint-stock banks, and many of the securities they are prepared to accept would not be acceptable to the latter. But they are enabled to do so without much risk on account of their greater personal knowledge about their clients. Thirdly, they also buy and sell remittances, and discount hundis. Fourthly, they finance the movement of crops from the villages to the inland trade centres. Lastly, they may purchase produce and act as the purchasing or distributing agent of the big mercantile firms.

The indigenous bankers still follow the traditional methods in regard to their banking business. They keep accounts according to the vernacular systems, and their principal instrument is the *hundi,* or the internal bill of exchange drawn up in a flowery language. These hundis carry a high rate of interest varying from 7 to 9 p.c.

Indigenous bankers and joint-stock banks. The indigenous bankers rely principally on their own funds to finance their operations. Hence they can afford to quote rates of interest which are not much related to the rates prevalent in the organised sector of the money market. But there are occasions when some contact is established between these

bankers and the joint-stock banks. When these bankers are hard-pressed for funds to finance the movement of crops, they rediscount some of their *hundis* with the State Bank and other joint-stock banks. The latter generally advance loans and provide rediscounting facilities to these bankers who are on their approved lists upto certain limits determined with reference to their financial standing. During such periods a bridge is established, at least temporarily, through which funds from the organised sector pass into the indigenous part of the money market.

The indigenous bankers and the Reserve Bank. The indigenous bankers have no direct contact with the Reserve Bank, except that some among them (8 in number in March 1958) have been granted the facility of remitting funds through the Reserve Bank at concessional rates. The history of the efforts made by the Reserve Bank to forge a direct link between it and these bankers in 1937 and 1941 has been discussed in an earlier chapter. In 1954 the Shroff Committee recommended that the Reserve Bank should make another attempt to establish a link with these bankers. In a Note dealing with this subject, the Reserve Bank reviewed the whole position. There have been two changes since the year 1941. First, there has been a tendency on the part of some indigenous bankers to convert themselves into joint stock banks. Secondly, with the increase in the number of branches of banks, especially of the State Bank of India, these bankers have been able to obtain funds from joint-stock banks at reasonable rates. It has been suggested that the Reserve Bank should rediscount the usance bills of indigenous bankers, such as the *multani hundis* of Shikarpuri shroffs through the scheduled banks. In the opinion of the Reserve Bank, the extension of this privilege of rediscounting to *multani hundis* would not be of much significance except theoretically. The purpose behind this proposals is to provide banks which rediscount these hundis with additional funds. But the principal banks which undertake this business could easily borrow from the Reserve Bank, if necessary, against other usance bills and government securities if they wanted more funds to take up the *multani hundis*. "There is, therefore, no justification for the creation of an elaborate machinery for the rediscount of these *hundis*, when the object can be achieved very simply under the present system."

Comments. Since these firms are family concerns the influence of tradition is very strong on their working methods. The banker is brought up to his calling, and relies mainly on the experience of his

family in the past. Hence these bankers are disinclined to introduce modern methods into their business. Their accounts are kept in a simple and economical way, but are unsuitable for purposes of audit by modern accountants. They charge comparatively high rates of interest. These are no doubt important defects.

But against all these one must remember thai any one conducting business with these bankers would not have to face too many formalities and delays, which are sometimes inevitable in one's dealings with joint-stock banks. They are also easily accessible, and their lending policy is highly flexible. They are prepared to lend against securities which would not be touched even with a pair of tongues by the joint-stock banks. Moreover, the indigneous banker offers special facilities to his customer. He is prepared to open up for business at 6 a.m. in the morning and remain in his office till late in the evening. They are, therefore, available at hours when joint stock banks aie closed. Because of these facilities, even large firms have been found to be keeping accounts with indigenous bankers.

Insurance Companies : In the western countries insurance companies, which gather the personal savings of the people, have come to occupy an important position in the capital market. In India also, they are gradually playing an incresing role in supplying investible funds to the money market. Thus the annual amount of new funds available at the disposal of all life insurance companies in India has increased from Rs. 7·14 crores in 1939 to Rs. 15·49 crores in 1945 and to Rs. 27·05 crores in 1952. These funds are invested in government securities, industrial securities, mortgages etc. Thus they provide an increasing amount of funds for purposes of investment.

The aggregate assets of all insurance companies amounted to Rs. 295·37 crores in the end of 1952. Of these 46·9 p.c. (*i.e.* Rs. 138·52 crores) were invested in government securities, and 14·1 p.c. (*i.e.*, Rs. 41·79 crores) in shares and securities of joint-stock companies. During the post-war period, 1945-1952, out of an annual average increase of Rs. 22·44 crores, only 32 p.c. were invested in government securities and 18·3 p.c. went into the shares and securities of joint-stock companies. This was no doubt a welcome trend. But the percentage of investment in industrial securities by Indian insurance companies was definitely lower than that in the U.K., and the U.S.A., where investment of life insurance funds in industrial securities amounted to 29·9 p.c.

and 43·1 p.c. respectively. The Indian companies were, of course, not free to invest their funds in any way they like. Their discretion was restricted by the provisions of the Indian Insurance Act. But they should re-orientate their policy and invest a larger proportion of their funds in industrial securities so that more funds become available for the development of industries in this country.

Recently the government has nationalised the life insurance business, and all companies dealing in life insurance have been taken over by the government. To administer these companies the government has formed a Life Insurance Corporation, which is now the authority for the investment of the large funds accruing to the Corporation from its premium income. Thus a large part of the total investible funds of the country is now under the control of the government.

According to the latest available report of the L.I.C., it had completed new business worth Rs. 997·5 crores in 1960, as compared to Rs. 255 crores in 1955, the year before nationalisation. The annual premia collected have increased from Rs. 58·55 crores in 1955 to Rs. 96·9 crores in 1960, *i.e.*, an increase by 65%. The L I C have recently adopted a new scheme to popularise insurance in rural areas, under this scheme, policies upto Rs. 2000 are issued to residents without medical examination in selected rural areas.

Questions

1. Discuss the relation of the State Bank of India to the State and the Reserve Bank of India.

2. Outline the recent trend in Indian banking. What is the part that the Reserve Bank has played in the development of sound banking in the country ?

3. Describe the position of the exchange banks in the import and export trade of India. Do you advocate the imposition of any restrictions on their operations ?

4. Describe the position and functions of the joint-stock banks in the Indian money market. In what relation do they stand with the Reserve Bank of India ?

5. Describe the organization and functions of indigenous bankers. By what methods, if any, can they be brought within the organised banking system ?

CHAPTER 37.

SOME PROBLEMS OF BANKING

We have already surveyed the structure and working of the chief constituents of the Indian money market. In this chapter we shall discuss some problems of banking like the defects in the working of the banking system, the question of banking legislation, the necessity of deposit insurance, and the problem of the extension of banking facilities etc.

Defects of the banking system : India now possesses a well-developed banking system which has stood the test of several crises like a depression, a war and a partition in a remarkable manner. There are a number of banks which are sound in organisation and are run in an efficient manner. They compare very favourably with some of the British or American banks. Just as in Great Britain, there are the big four banks (*viz.*, the Central Bank of India, the Bank of India, the Punjab National Bank and the Bank of Baroda) which dominate the money market.

But in spite of this impressive advance, several serious defects can be found in the structure of the banking system. In the first place, a large number of banks work with very small or inadequate capital and do not possess proper reserves. Even in 1953, one scheduled bank and 28 non-scheduled banks had no reserves at all. At the end of 1953, there were 49 banks whose paid-up capital and reserves were less than Rs. 50,000.

Secondly, a number of defects were stated in the first Report on the Trend and Progress of Banking (1949), issued by the Reserve Bank. That report pointed out that

(*a*) Some of the directors of banks lacked the knowledge and experience necessary for running the banks. In a few cases, the system of internal audit and inspection was defective. A number of banks followed the wrong practice of declaring dividends without making adequate provisions for bad and doubtful debts, depreciation in investments, etc.

(*b*) There were also important defects in the investment policy of some of these banks. Some banks lent heavily against the shares of companies in which some of the Directors were interested and also against shares which were not readily marketable. In some other cases investment in government securities was low in proportion to the resources.

(*c*) The advances granted by some banks were entirely unwarranted by their resources. Some of them also failed to observe the salutory principle of diversification of risks in course of their lending operations. They have not also exercised proper care in investigating the credit-worthiness of the borrowers.

(*d*) In the case of some banks adequate supervision was not kept over the activities of branches, and regular returns of advances etc., were either not called for or not properly scrutinised at the head office.

Lastly, apart from these internal defects, another disquieting feature is the want of any organisation for keeping watch over, and improving banking standards. The absence of such an organisation and the lack of co-operation among banks themselves in the matter of mutual assistance provide evidences of the defective growth of the system.

Bank failures : The rate of mortality among the banks has been causing grave concern to everybody. The following table from the *Banking and Monetary Statistics of India* (Reserve Bank of India) will show the extent of bank failures in India. The table shows that beginning from 1913 from which year statistics have been published, bank failures have occurred in every year, the number of bank failures varying from, as low as 3 to as large as 117. As the table would be too long for publication in this book, we have selected some particular years to show the trend of bank failures.

TABLE I

Bank failures. Number and Paid-up Capital

Year	Number	Paid-up Capital
1914	42	Rs. 1,09,02
1919	4	Rs. 4,03
1923	20	Rs. 4,65,47
1928	13	Rs. 23,12
1934	30	Rs. 6,23
1935	51	Rs. 65,96
1939	117	Rs. 24,91
1940	107	Rs. 23,90
1945	27	Rs. 4,74
1948	45	Rs. 1,79,32
1949	33	Rs. 1,17,05
1950	45	Rs. 1,40,19
1951	62	Rs. 62,09

In 1948, 1949, and 1951, the largest number of failures took place in West Bengal. In 1948, 20 out of 45 banks, in 1949, 27 out of 33 banks, and in 1951, 39 out of 62 banks closed their doors.

The failure of the Palai Central Bank of Kerala and a number of other banks in 1959-60 has again brought this problem to the forefront.

Causes : The rate of bank failure, therefore, grew to alarming proportions in 1946 to 1951. What are the causes of such failures? These causes have been grouped into (*i*) internal causes and (*ii*) other causes.

The following are the causes arising out of internal factors (*a*) Inadequate capital resources have been an important factor in bank failures. A large majority of banks which have closed down had very low paid-up capital and practically no reserves. (*b*) Lack of experience and trained personnel has also been an important factor. If the history of some of the banks which failed is traced, it will be found that inexperienced persons who had been in search of a career organised a few banks and carried on so long as the conditions were favourable. But when any crisis came, they could not meet the situation. (*c*) Unsound investment policy. Some of these banks invested their funds in industrial shares for speculative purposes. In other cases short-term deposits were utilised in share market speculation. In fact stock exchange speculation undermined the financial stability of some of the banks which failed in West Bengal in recent years. (*d*) In many cases lending policy was also defective.

There have been cases of clean advances to Directors without any security. On other occasions Directors took advances for financing their own companies and as they could not repay in time, the banks naturally fell into difficulties. (*e*) Uneconomic branch banking has also been an important factor. Under the mistaken impression that banks with a large number of branches would command great prestige, there was some eagerness to open branches which landed many banks in difficulties as the expense ratio was thereby very much increased. Sometimes high rates of interest were offered to attract deposits in these branches, and to earn such rates, banks had to invest funds at high rates, and such investments were not always safe. (*f*) Above all, the Directors and Managers were not always honest. There were many

cases when Managing Directors, Directors or Managers utilised bank funds for their own purposes without regard for financial rectitude.

In addition to the above causes, there were also, from time to time, certain other general or special factors which adversely affected the position of the banks. For example, the collapse in the stock markets in 1946 undermined the position of many small banks in Calcutta, especially those which had traded unwisely.

Banking legislation : The large number of bank failures in different periods and the awareness of the defects of the banking system have agitated the public mind for a long time. Public attention was, therefore, drawn to the desirability of the statutory regulation of the activities of banks as early as 1913-14. The question was investigated in detail by the Central Banking Enquiry Committee of 1930-31, which recommended the passage of a comprehensive Bank Act. As banks were joint-stock companies, their organisations and functions were governed by the Indian Companies Act. But these provisions were entirely inadequate.

The necessity for such banking legislation is now admitted by everybody. It is of course true that good banking depends more on good bankers than on banking laws. But the reason why one wants banking legislation lies in the fact that not all bankers may be good, and that a large section of them would be influenced in the right direction and kept to the proper path by means of a judicious banking legislation. The business of banking is generally regarded as a public service, which should be properly regulated by law in the national interest. In many important countries like the U.S.A., Canada, Sweden, Switzerland etc., there are special banking laws. Such statutory regulation of banks has been considered necessary for the protection of the depositors and for ensuring the development of banking on lines which experience has proved to be sound.

History in India: The first attempt at banking legislation was the passing of the Indian Companies (Amendment) Act, 1936, which embodied some of the recommendations of the Central Banking Enquiry Committee. That Act gave a definition of banking and laid it down that a banking company must restrict its business to banking only. It prohibited the employment of managing agents in banking companies. Every bank must have a paid-up capital of at least Rs. 50,000 before it

would be allowed to commence business. Every bank other than a scheduled bank must keep at least 20 p.c. of the profits in the reserve fund before any dividend could be declared. The reserve fund was to be accumulated in that way until it became equal to the amount of paid-up capital. The reserve fund is to be kept invested in government or trustee securities or deposited with a scheduled bank. Every bank other than a scheduled bank must keep a cash reserve of at least 1½ p.c. of its time liabilities and 5 p.c. of its demand liabilities. Banks were prohibited from acquiring shares in subsidiary companies other than a subsidiary concern of their own.

Within a short time these provisions proved inadequate and difficult to administer.

The failure of the Travancore National and Quilon Bank in 1938 and the subsequent banking crisis in South India agitated the public mind. The Reserve Bank submitted a draft Banking Bill to the government in November, 1939. The draft Bill was circulated for public opinion, but the government decided not to proceed with it during the war. However, an amendment was passed to the Indian Companies Act in 1942 by which a proviso was added that any company using the name "bank", "banker" or "banking" would be deemed to be a banking company.

The years 1942 and 1943 saw the floatation of a number of banks whose capital structure and terms of managerial appointments were considered undesirable. So the Reserve Bank prevailed upon the government to amend the Indian Companies Act. These amendments prohibited a bank from issuing anything except ordinary shares or such ordinary and preference shares as were issued before the commencement of the Act. The subscribed capital of the bank should not be less than half its authorised capital and the paid-up capital must be at least half its subscribed capital. No bank would be allowed to employ a person whose remuneration took the form of a commission or a share of profits or a person having a contract for its management for more than 5 years. The voting rights of the shareholders should be in proportion to the contribution made by them to the paid-up capital.

In 1944 the Reserve Bank revised the original draft Banking Bill, and the government introduced the Banking Companies Bill in the

Parliament. The Bill was referred to the Select Committee. But before that Committee could meet, the Legislative Assembly was dissolved, and the Bill lapsed. But the government promulgated the Banking Companies (inspection) Ordinance, 1946, which empowered them to direct the Reserve Bank to carry out the inspectinn of the books and accounts of any bank.

After the new Assembly was elected, the government introduced another Banking Companies Bill in 1946. The Bill was referred to the Select Committee. In the meantime as the indiscriminate expansion in branch-banking was considered undesirable, the government passed the Banking Companies (Restriction of Branches) Act in 1946. This Act required banks to obtain the permission of the Reserve Bank before opening new branches or changing the location of existing branches.

The consideration of the Banking Companies Bill, as amended by the Select Committee, could not be taken up by the Constituent Assembly on account of a large number of amendment necessitated by constitutional changes. The old Bill was withdrawn and a fresh Bill was introduced in 1948. As there was some delay in enacting this legislation, the government passed the "Banking Companies (control) Ordinance in 1948, containing some of the important provisions of the Banking Companies Bill. The Bill was finally passed in February, 1949, and came into force from 16th March, 1949.

The Banking Companies Act of 1949*: The Banking Companies Act is a comprehensive piece of legislation designed to regulate the operations of banks. In order to distinguish between banking and non-banking companies, it defines the term, "banking," as "the accepting, for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise, and withdrawable by cheque, draft, order or otherwise." (*a*) A bank must take out a licence from the Reserve Bank of India before the commencement of business. All existing banks would have to apply for licence and would be entitled to carry on business until a licence was refused to it. (*b*) Banks would have to satisfy certain minimum capital requirements. Every bank must have a minimum capital of Rs. 50,000. The following table will show the minimum paid-up capital and reserves of different types of banks.

* This Act is now known as Banking Regulation Act.

TABLE II

Types of Banks	*Minimum paid-up capital and reserves*
(*a*) All branches in one State, not being Calcutta or Bombay.	Rs. one lakh plus Rs. 10.000 for branches in the same district, plus Rs. 25,000 for branches in other districts in the same State.
(*b*) All branches in the States of Bombay or West Bengal including one at Bombay or Calcutta.	Rs. 5 lakhs plus Rs. 25,000 for each branch outside Bombay or Calcutta.
(*c*) Branches in more than one State, excluding Bombay or Calcutta.	Rs. 5 lakhs.
(*d*) Branches in more than one State with one at Bombay or Calcutta.	Rs. 10 lakhs.
(*e*) Banks incorporated outside India.	Rs. 15 lakhs or Rs. 20 lakhs if it has an office at Calcutta or Bombay.

Existing banks must comply with these requirements within 3 year. These provisions were meant to prevent the growth of mushroom banks with inadequate capital structure, and to regulate the opening of branches. To achieve the latter purpose, it was further laid down that banks would have to take the permission of the Reserve Bank before opening new branches or changing the existing location of old branches. (*c*) No bank can appoint a person as managing agent, nor can it appoint any person as the Director who is already a Director of another bank. (*d*) No bank shall form a subsidiary company except one formed to carry on functions incidental to the business of banking. It must not hold shares in any company of an amount exceeding 30 p.c. of the paid-up share capital of that company or 30 p.c. of its own paid-up capital and reserves, whichever is less. (*e*) It shall not make any loans or advances on the security of its own shares or grant unsecured loans to any Director to firms or private companies in which it or any of its Directors is interested as a partner or managing agent. (*f*) Every bank must maintain a reserve fund and transfer at least 20 p.c. of its profits to this fund every year until the reserves become equal to the paid-up capital. (g) Every bank, not being a schedule bank, must maintain by way of cash reserve a sum equal to five per cent of its demand

deposits or two per cent of its time deposits either in a cash with itself or in an account with the Reserve Bank or in both. In order to enable the Reserve Bank to verify whether it is doing so or not, the bank must send to the Reserve Bank 3 copies of a statement of the amount so held on Friday of each week with particulars of its deposits. (*h*) Every bank must maintain in cash, gold or unencumbered approved securities a sum equal to at least 20 p.c. of its total deposits. Existing banks would be given two years' time to comply with these requirements (*i*) Every bank must maintain assets equal to 75 p.c. of its total deposits in India at the close of the last working day of each quarter. (*j*) Every bank must submit to the Reserve Bank (*k*) monthly statements of its accounts, assets and liabilities, and (*l*) annual audited balance-sheets and profits and loss accounts. Such balance sheets are also to be sent to the Registrar of Joint-Stock Companies.

The Act also confers other powers of control on the Reserve Bank of India. Thus the Reserve Bank may determine the lending policy to be followed by banks or any particular bank if that is necessary in the public interest. It may also give directions to banks or groups of banks or any bank as to the purposes for which advances may or may not be made, the margins to be maintained in respect of secured advances and the rates of interest to be charged on advances. It may prohibit or restrict the grant of loans by a bank to any of its Directors if it finds that such loans are being granted to the detriment of the interests of the depositors. The Reserve Bank may call for any information relating to the business of a bank. It may, and on being directed by the Central Government, must inspect the books and accounts of a bank, and submit a report to the government. The government may, after consideration of the report and of any reply given by the bank, prohibit the bank from accepting fresh deposits, or direct the Reserve Bank to wind up the bank. The Reserve Bank may caution or prohibit any bank or banks against entering into any particular transaction or class of transactions and generally give advice to the bank.

The Act also contains certain provisions in connection with the suspension of business and winding up of a bank by the order of the courts. The courts are required to seek the opinion of the Reserve Bank before sanctioning any such prayer for suspension or winding up of business or for the amalgamation of banks.

Two major amendments to the Banking Companies Act were passed in 1950 and 1953. The former amendment clarified certain sections, and revised or simplified the procedure for the amalgamation of banks. The revised procedure is intended to encourage bank amalgamations without recourse to courts of law, by minimising the legal formalities and by eliminating the possibility of a few dessenting shareholders holding up the scheme. The amendment also sought to speed up the disposal of winding up procedure.

The amendments made in 1953 by the Banking Companies (Amendment) Act were passed to give effect to the recommendations of the Banks' Liquidation Proceedings Committee. These sought to simplify and speed up the liquidation proceedings, laying down a summary procedure for the realisation of the outstanding debts of a bank etc.

Comments on the Act : Some writers have complained that the Banking Companies Act puts the Indian banking system into a straight-jacket, and that it has granted wide and sweeping powers of control to the Reserve Bank. There is no doubt that some of the provisions were not necessary, and could be easily deleted, thus doing away with some of the complications of the Act. For example, since the Reserve Bank has been given blanket powers of control over the opening of branches, there was no more necessity for incorporating provisions under which banks were required to increase their paid-up capital for each branch. The Reserve Bank's powers are of course wide. But normally no soundly managed bank need be afraid of the application of these sections by the Reserve Bank. The weak and the erring banks should rightly be afraid of these provisions. From the last four or five years of working of the Act, there is every indication that the Reserve Bank is proceeding cautiously and wisely in the application of powers entrusted to its care. Its powers of inspection are being utilised to throw the spot-light of publicity and criticism on the weak spots in the banking structure. In a large number of cases exemptions from the more onerous sections of the Act have been granted to banks in order to save them from difficulties without defeating the purpose of the legislation. On the whole the Act has proved to be a beneficial piece of legislation, which is likely to strengthen the foundation of the banking system.

Banking Companies (Amendment) Act, 1956 : The administration of the Banking Companies Act of 1949 had brought to light

certain loopholes in the law in dealing with managerial irregularities of banks. Under the amendment, the appointment of the managing director, or wholetime director, or manager of a bank can only be made with the previous sanction of the Reserve Bank. The Reserve Bank may also prohibit the payment of remuneration to the top officials of the banks which it considers to be excessive. The Reserve Bank may also appoint observers to watch and report on the conduct of affairs of a bank, which may be required to make such changes in its management as may be considered necessary by the Reserve Bank. The latter may also issue directives to banks in relation to matters of policy or administration in the national interest or in the interest of the institutions themselves. The Act also extends the powers of the Reserve Bank to obtain statements and information relating to the business or officers of a bank. Certain other amendments are aimed at the prevention of the misuse of voting rights through the concentration of shares in the hands of a few. No director of a bank can become the director of another bank.

Banking Companies (Amendment) Act, 1962*: In the last few years the large demand for bank credit and the consequent increase in the total volume of bank advances have led to a lowering of the liquidity of the banking system. To cope with this situation, the government has passed a new amendment to the Banking Companies Act, under which banks would be required to maintain at least 25 p.c. of their total deposits in the form of cash, or gold, or unencumbered approved government securities, in addition to the 3 p.c. of the deposits to be kept with the Reserve Bank. As some banks might find it difficult to comply with this requirement immediately, this provision is to come into effect from September, 1964.

Insurance of bank deposits : The large number of bank failure in this country has drawn the attention of a number of writers to the need for introducing a scheme for the insurance of bank deposits. A proposal to that effect was placed before the Rural Banking Enquiry Committee, which thought that banking developments in India had not reached the stage when such a scheme could be adopted. The Shroff Committee of 1954 has, however, given a favourable consideration to the proposal, and has urged that its potentialities should be examined

* Provisions of the Banking Laws (Application to Co-operative Societies) Act, 1966 have been noted in the chapter on the co-operative movement.

by the authorities concerned. The recent failure of the Palai Central Bank has again revived interest in this proposal.

A scheme for the insurance of bank deposits has been first introduced in the U.S.A. under the Banking Acts of 1933 and 1935. With the onset of the world trade depression the American banks were passing through crisis, and large numbers of them had to close their doors during these years. The scheme of deposit insurance was devised to inspire confidence in the banking system. Under the scheme a Federal Deposit Insurance Corporation (FDIC) was established with its capital subscribed by the Treasury and the Federal Reserve Banks. Banks participating in the scheme had to pay premia to the FDIC at the rate of 1/12 of 1 p.c. per annum upon their total net deposits. In return, the FDIC insured all depositors in these banks against loss of deposits through bank failures upto the maximum of $5,000 per depositor. Thus depositors were given an assurance that even if banks failed, they would be paid upto a maximum of $5,000 by the FDIC. The scheme was thus designed to recreate the confidence of small depositors in the banking system and so prevent hasty and panicky withdrawal of bank deposits.

In has, therefore, been urged that the introduction of such a scheme in India would increase the confidence of the people in the banking system which has been rudely shaken by the failure of 187 banks over the 1947-52 period, involving a loss of Rs. 92 crores. A Deposit Insurance Corporation should be introduced in India with capital subscribed by the government, the Reserve Bank and other financial institutions. It should collect premia from all banks registered under the Banking Companies Act, and provide insurance for all depositors in banks upto a maximum of (say), Rs. 5000 per depositor. A lower limit would not also matter very much as the average deposit per account in India varies between Rs. 1,500 and Rs. 2140. The payment of this premium will of course result in the imposition of an additional burden on the banks which have already to put up with high operating costs on account of various banking awards. But the scheme will allay the fears of moneyed people regarding the safety of their funds and so is likely to increase the volume of bank deposits. This will, therefore, offset the increased costs due to the payment of the premia.

It has, however, been urged that the scheme is not practicable in India at the present stage. As the Rural Banking Enquiry Committee

stated, "the risks and uncertainties to which banking in this country is subject at present are far too many and their nature is not yet fully understood." The risks of bank failures in this country are not calculable and one cannot anticipate beforehand the financial burden it may involve in the future. The process of consolidation of the banking system through the weeding out of uneconomic or inefficient or dishonest units has only been started since the passage of the Banking Companies Act, and so long as this does not go to the extent necessary to make the risks of bank failure a calculable one, it would not be correct to introduce the scheme in our country. With the introduction of such a scheme, the authorities may be lulled into a false sense of complacency, especially if, during the initial stages, the number of bank failures remains low due to some good luck. They may not then keep a careful watch over the weak links in the banking system.

The failure of the Palai Central Bank and a number of other banks has again revived the question of insurance of deposits. This was examined by the Reserve Bank and the Government of India when it was decided to introduce a scheme in this country. It has been decided to establish a separate autonomous corporation for this purpose.

The Deposit Insurance Corporation has been established as from January, 1962. It has an authorised capital of Rs. 1 crore, which is fully paid-up by the Reserve Bank of India. The Board of Directors of the Corporation consists of five members,—the Governor of the Reserve Bank who is the Chairman, a Deputy Governor of the Reserve Bank nominated by the Reserve Bank, an officer of the Central Government nominated by them and two directors nominated by the Central Government, having special knowledge of commerce, industry or finance. These two directors must not be connected with any bank, and are to function for a period of 4 years. The Board shall constitute an Executive committee from among themselves to conduct the day-to-day affairs of the corporation. The Corporation must follow the policy laid down by the Central Government after consulting the Reserve Bank.

All commercial banks are to be insured and the amount of deposits to be covered by insurance has been fixed at Rs. 1500 per depositor in each bank. This amount may be raised from time to time with the prior approval of the Central Government. The maximum premium which may be charged has been fixed at 15 P. per year for every Rs. 100 of the total deposits of a bank. For the present the rate of

premium has been fixed at 5 P. per year per Rs. 100 of deposits, *i.e.*, at 1/20 of 1 p.c. of deposits. When an insured bank closes its doors the liquidator of the bank shall furnish a list of depositors to the Corporation within 3 months, and the Corporation shall pay the depositors within the next 2 months. The Corporation will not carry out any inspection of any bank. This is carried out by the Reserve Bank of India. The Corporation may, however, request the Reserve Bank to inspect an insured bank and furnish it with copies of the inspection reports. The insured banks have also been required to supply the Corporation with any information relating to their deposits.

Since its inception in 1962 to the end of March, 1966, the Corporation has insured about 115,76 lakhs accounts with the insured banks out of which about 77 p.c. were fully insured, having balances not exceeding Rs. 1500. It has met claims aggregating Rs. 38·59 lakhs in respect of 9 banks.

Extension of banking facilities to rural areas : We have already seen in connection with the discussion of the indigenous bankers that while India possesses 3018 towns and 558089 villages, the offices of joint-stock banks numbered only 4192 in 1956. Most of the banking offices are concentrated in cities and the larger towns. It is doubtful whether there are any banking offices in the villages. Thus from this point of view banking facilities are inadequate, especially in the rural areas of the country. The villages are served at present by the Post Office Savings Banks, the money-lenders and the co-operative credit societies. The latter are of course helping to spread thrift and banking habits. But their number is as yet not large enough to cover all the villages. Moreover, not all credit societies are in a sound condition. Post Office Savings Banks only collect the deposits from the public, but do nothing else for the spread of banking habits.

Joint-stock banks should, therefore, think of opening branches in the village. Such a step bristles with certain difficulties. One is the uncertainty of securing enough business in the rural branches to pay for the expenses. It is doubtful how far the banks would be able to collect rural savings. In the first place, the vast majority of the villagers are too poor to save anything out of their meagre incomes. Those who have some savings are not likely to deposit them with the banks for two reasons. One is the illiteracy and the conservatism of these people, as a result of which few of them have clear ideas about banks and

banking in general. The other is the possibility of earning elsewhere higher rates of interest than are paid by joint-stock banks on their deposits. Lastly, banks have urged that on account of the various banking awards, their operating costs have risen so high that it would no longer be profitable to open branches even in the ordinary towns, not to speak of the villages.

The question of extending banking facilities to the rural areas was first examined by the Rural Banking Enquiry Committee of 1950. That Committee has recommended a number of measures for the purpose of extending banking facilities to the rural areas. The Imperial Bank (now the State Bank), should be asked of open more branches in the rural areas, and should at least have one branch in every taluka headquarter. The government, should, if necessary, pay some subsidy to the State Bank in order to enable it to open more branches. In order to encourage other banks to open branches in the villages, the Reserve Bank should provide them with the maximum facilities for the cheap remittance of funds that they may send the funds collected in the villages to their head offices or other centres in need of funds. They should also be given adequate facilities for keeping their currency chests for safe custody in the strong rooms of treasuries and sub-treasuries. The Committee further proposed that bank branches situated in towns containing less than 50,000 people should be exempted from the application of Banking Awards and the Shops and Establishments Act. It also made a number of recommendations for improving the services of the postal savings banks. Lastly, it recommended the establishment of a Warehousing Development Board with funds supplied by the Central and State Governments and the Reserve Bank for the purpose of establishing warehouses in different parts of the country.

In 1954, the Report of the Committee on Rural Credit Survey made a number of recommendations for encouraging the growth of banking in the rural areas. The most important recommendation was the nationalisation of the Imperial Bank of India. This has already been done, and the Imperial Bank has been re-named the State Bank of India. The State Bank has been placed under obligation to open at least 400 branches in different localities within the next five years. This had already been done. The idea is to create one strong, integrated, state-sponsored and state-partnered commercial bank with an effective machinery of branches spread all over the country which are to provide vastly extended

remittance facilities for the co-operative banks, and thus stimulating the further establishment of such banks in the rural areas.

At the village level, there should be a definite plan for the development of co-operative banks on a wide scale to cover as large area as is possible. These co-operative banks are to be organised on a larger basis with 51 p.c. of their capital beings subscribed by the State government. These co-operative banks are to be federated into the central co-operative banks, which, again, are to be organised into the State Co-operative Bank. At each stage, the State government should contribute to the share capital of these banks and take part in their management. Side by side with these banks, the State should organise a chain of warehouses and godowns in the country where crops are to be stored and certificates of deposit are to be issued. If the storage and warehousing programme is successfully carried out, commercial banks will then be able to lend against the warehousing receipts as these receipts can be discounted with the Reserve Bank. The extension of the branches of the State Bank of India into the rural areas, and the provision of cheap remittance facilities by the latter, combined with the establishment of warehouses will make it possible for the commercial banks to embark on large branch expansion themselves. In particular, the scheme of starting "mobile banks," maintained and run by the commercial banks, might be given a trial in areas where there is no near prospect of the development of co-operative credit.

This is, more or less, an outline of the integrated scheme put forward by the Committee on Rural Credit Survey. The scheme has of course a number of good features as it provides not only for the strengthening of the basic organisation,—the co-operative banks, but also for forging a link between the base and the apex organisations. The State Bank with its extensive branches will prove to be a tower of strength to the whole system. The commercial banks cannot be expected to establish a large number of branches in the rural areas unless these places are covered with a network of warehouses. Even then they can lend only to large producers, and the vast majority of the rural population are mainly small producers. Hence the provision of banking facilities in the rural areas will have to be based on the co-operative system.

Nationalisation of Commercial Banking : The demand for the nationalisation of commercial banks has become insistent since the nationalisation of the life insurance companies and the Imperial Bank of India. The government, it is claimed, should take over all the

commercial banks of the country as it had done in the case of the Imperial Bank. After nationalisation, the organisation of the Imperial Bank has been much improved, and the State Bank of India has opened a large number of branches in the rural areas and has adopted such beneficial measures as the financing of small-scale industries. It is not conceivable that the Imperial Bank of India would have agreed to do all these things under the old management. The nationalisation of that Bank has, therefore, served to broaden its objectives and to enlarge its activities. The same thing will happen, it is argued, if other banks are also nationalised. The extremely conservative ideas of the present management of these banks can be replaced by more progressive ideas with beneficial effects on the economy. The resources of these banks can then be utilised to start more branches all over the country, to provide more funds towards financing small business units and in other desirable directions. These may not be regarded as credit worthy by conservative banking standards. But after nationalisation, with the pooled resources of so many banks it may become possible to assume larger risks in the real interests of the country.

Another important argument in favour of nationalisation is that monopoly capitalists have been able, through these private commercial banks, to increase their hold upon the industrial and trade sectors. Many of these banks have been started by the industrialists themselves who have utilised their large deposit resources in promoting their own selfish objectives. There is too much interlocking of directorates between these banks and the large industrial combines and their managing agency firms. So these banks are helping the process of concentration of economic power among a few families. Nationalisation will put an end to this process, and may thus prove to be an important means for remedying the growth of monopolies and the concentration of economic power.

Another idea behind the demand for nationalisation of banks is that this measure will enable the government to get hold of the resources of these banks for the financing of the different economic plans. This will therefore mean less recourse to higher taxation and to deficit-financing, and may thus prove to be an important anti-inflationary factor. The anti-inflationary effect may come in another way. Though the Reserve Bank is exercising control over the operations of these banks, usually so many loopholes exist in all control regulations that banks have not found it difficult to satisfy the banking needs of the

speculators and hoarders, many of whom are old customers of the banks or have intimate business relations with Directors of the banks. The activities of these speculators and hoarders have been an important factor in bringing about the present rise in prices. Only by nationalisation will it be possible to plug these loopholes and stop the flow of banking funds to these speculators and hoarders ?

Those who oppose such nationalisation point attention to the defects of institutions which have already been taken over by the State, *e.g.*, the State Bank of India on the LIC. Everyone knows the large amounts of complaints against the LIC, the inevitable delays, the redtapism and the other unsatisfactory state of affairs. The State Bank has no doubt opened many branches. But this has been possible because of the grant of subsidy on losses entertained by the Bank on unremunerative branches. The State Bank has never been noted for its services to the depositors ; there is too much delay in the payment of cheques, too many formalities, and the very impersonal manner of handling customers. Private management has ensured an efficient, strong and effective banking service to the country. and all this will be lost if the banks are nationalised. If there are still defects or complaints against particular banks, these can easily be handled by the machinery of the Reserve Bank of India, which, as it is well-known, exercises almost dictatorial powers over these banks. The growth of monopolies or the concentration of economic power and wealth is the inevitable result of the present economic system, and it cannot be remedied through the creation of another gigantic monopoly in the shape of a nationalised banking organisation. That will not serve to revive competition for providing better services to the depositors and other customers. The buyers of life insurance are not getting better services from the LIC than they were from the highly competitive life insurance companies. Though the same complaints regarding misuse of funds, speculative loans etc. were raised against the life insurance companies before nationalisation, nobody will say that things have gone even a shade better in these respects after the nationalisation of these companies. At least in India, the nationalised public corporations have become the *Varanasi* of old, retired officials (mostly of the ICS variety), there is no reason why the banking organisation, which is a highly competitive and sensitive organisation, should be reduced to that status for no fault of its own.

The argument that nationalisation of banks will bring in more revenues to the coffers of the State is absolutely unsupportable. In fact, the nationalisation of the Imperial Bank or the life insurance companies has not augmented the revenues of the government. The government will have to pay suitable compensation to the shareholders at the market rates, and this will eat up almost all the profits of these companies, and if to this is added the fact that the expenses of running the governmental or semi-governmental administrative machineries are generally much higher than those of a privately-managed concern, there will be little hope of getting any additional revenue from the nationalised banks. Nationalisation of bus services has not served to bring in any revenue to the State governments in spite of high expectations.

Nationalisation of commercial banks is, therefore, a highly risky measure. In the UK, the Labour government has nationalised many sectors of the British economy without nationalising commercial banks. The reasons are quite obvious. Such a measure is neither necessary nor desirable in a mixed economy like ours.

Questions

1. What are the defects of Indian banking system ? Suggest suitable remedies.

2. Account for the large number of bank failures in West Bengal in recent years. What measures would you suggest for preventing such failures in the future ?

3. What are the causes of bank failures in India ? Do you advocate the insurance of bank deposits ?

4. Discuss the necessity or otherwise of enacting legislation for regulating banking in India.

5. Discuss the factors which impede the extension of banking facilities in India. What measures would you suggest for the development of such facilities ? (C. U. B. Com. 1957).

6. Examine the main provisions of the Banking Act of 1949. Describe the principal measures which have been adopted recently to put the banking system on a sounder basis.

7. Examine recent legislation for regulating banks and sugggest improvements.

8. Examine the scope for the extension of banking facilities in the rural areas of India. What are the obstacles that stand in the way of such extension ?

CHAPTER 38

PRICE MOVEMENTS SINCE THE WAR

War-time rise in prices : When the second world war broke out in September, 1939, Indian prices were just recovering from the previous recession of 1937-38. The index number of Calcutta wholesale prices, which had fallen to 95 in 1938 from 102 in the previous year, had again risen to 100 in August, 1939. The war then intervened and prices started rising. For purposes of studying the trend, the movements in the index numbers of prices are exhibited in the following table.

TABLE I

Price movements during the war, 1939-45.

Economic Advisers' General Index : Base=Aug. 39=100.

Months	1939-40	1940-41	1941-42	1942-43	1943-44	1944-45	1945-46
April ..		125·6	116·1	146·1	227·6	234·6	242·3
May ..		120·8	121·5	148·4	236·4	237·4	238·1
June ..		110·3	130·2	155·2	241·4	239·7	237·4
July ..		112·1	140·9	159·9	239·0	245·3	244·4
August ..	100·3	108·4	142·5	160·0	237·9	245·0	244·1
September ..	108·2	111·1	142·2	164·3	236·3	243·3	242·2
October ..		112·1	142·1	171·4	240·8	243·4	244·1
November ..		115·7	146·5	177·0	239·1	246·5	243·6
December ..	137·8	114·4	140·0	184·7	234·8	249·2	247·1
January ..		114·8	145·0	190·4	237·0	250·3	250·2
February ..		111·1	145·1	197·6	235·7	248·8	252·8
March ..	127·5	118·8	145·6	213·5	232·1	247·8	253·3
Average for the year ..	126·0	114·9	136·8	171·4	236·5	244·2	244·9

The immediate declaration of the war gave a spurt to the rise in prices which increased from 100·3 in August, 1939 to 137·8 in December, 1939. Most of this rise was speculative, and gradually prices began to fall until they came down to 108·4 in August, 1940. Thereafter

the rise in prices was almost continuous, with occasional small breaks, until we come to the month of October 1943, when the index number stood at 240·8. The end of this financial year saw a small decline in prices to 232·1 in March, 1944. But next year prices rose almost continuously, though by a small percentage, *i.e.*, 3 p.c. in 1944-45 as against a rise of 38 p.c. in 1943-44 and 25 p.c. in 1942-43. In 1945-46, the index number, after falling to 237·4 in June, 1945 from 247·8 in March, 1945, rose at the end of the year to 253·3.

Thus during these war years, 1939-45, Indian prices had risen from 100 to 247·8 in March, 1945. As against this, wholesale prices increased in Great Britain from an average of 103·4 in 1938 to 172·2 in 1945. In the U.S.A. wholesale prices rose from 78·6 in 1938 to an average of 105·8 in 1945. In Canada prices rose from 107 in 1938 to 141 in 1945 and in Australia from 99 in 1938 to 146 in 1945. In everyone of these countries, the rise in prices during the war was much less than in India.

Causes. The main reason for this considerable rise in prices was the deficit financing in which the Government of India indulged throughout these years. The following table will show the extent of deficit financing resorted to by the Government of India between the period, 1939-40 and 1945-46.

TABLE II

Extent of Deficit Financing of the Central Government

Item	1939-40	1940-41	1941-42	1942-43	1943-44	1944-45	1945-46	Total
1. Deficit on Revenue Account ..	—	7	13	112	190	161	123	605
2. Deficit on Capital Account (Defence expenditure)		—	—	53	37	63	15	168
3. Recoverable war-expenditure ..	4	53	194	325	378	411	347	1,712
4. Total ..	4	60	207	490	605	635	485	2.485

Of the total deficits of Rs. 2,485 crores incurred during these years, not more than Rs. 800 crores were met by borrowings from the public.

The rest was met by the creation of new money. If we study the table closely, we shall find that the item, recoverable war expenditure, played the major role in the creation of deficit. Out of a total deficit of Rs. 2485 crores, Rs. 1712 crores were due to this item of expenditure. With the outbreak of the war the Government of India entered into a financial agreement with the British Government according to which it was laid down that while India would pay for its local defence, Britain would pay for all expenses incurred by the Government of India in the interests of wider imperial strategy. All liabilities of the British Government were settled by monthly payments of sterling to the account of the Government of India at the Bank of England. This item was known as the "recoverable war expenditure." The amount of sterling so received by the Government of India was transferred by it to the Reserve Bank of India, and the latter issued paper currency notes against these sterling balances and handed them over to the Government of India which spent the notes for meeting the war expenditure incurred on behalf of the allies. Thus the amount of sterling held in the two Departments of the Reserve Bank increased from Rs. 71·16 crores in 1939 to Rs. 1549·50 crores in 1946. Against this increase in sterling balances, the Reserve Bank increased its note issue from Rs. 182·36 crores in 1939 to Rs. 1,162·64 crores in 1946. Thus the increase in the sterling balances, in the amount of notes in circulation and in the price level was all the outcome of the heavy deficit financing by the Government of India.

While the large volume of deficit financing forced up prices, the position was aggravated by the appearance of bottlenecks in the production and supply of foodgrains. For example, in 1941-42, there was a failure of monsoons and a number of natural calamities like cyclones etc. This led to a large decline in food production. At the same time, the enemy occupation of Burma stopped an important source of supply of foodgrains. The result was a very steep rise in the prices of foodgrains. In the serious inflationary phase of the war, *i.e.*, in the year 1942-43, while the general index number rose in one year from 146·1 to 213·5, *i.e.* a rise of 67·4 points, the index number of rice prices rose from 169 in April, 1942 to 643 in April, 1943 ; that of wheat from 216 to 308 during the same period. The bottlenecks in the production of foodgrains thus caused a very large-scale rise in food

prices and so proved to be an important factor in driving up the general price level.

Thus as the war approached the frontiers of India, there was a great influx of allied armies into the country. Defence expenditures fed by deficit financing increased by large amounts. As a result, employment and money incomes rose to very high levels. For the first time the country was almost in the stage of full employment. While money incomes were thus soaring, the volume of goods available for civilian consumption could not keep pace on account of bottlenecks in production, restrictions on imports and shortage in capital goods. With no effective machinery for rationing and price controls, prices rose higher and higher.

Beginnings of control and rationing : In the early years of the war there was virtually no price control excepting the fixing of maximum prices of certain classes of goods. The period, April to July 1943, which witnessed a steep rise in prices, led to the gradual adoption of a number of direct economic controls. Measures were adopted in close succession for controlling the production and distribution of cloth, and for preventing hoarding and profiteering in general. Simultaneously an Ordinance was promulgated enforcing compulsory savings on those paying excess profits tax. An order seeking to control issues of capital came into force, the object being to prevent the floatation of companies which did not assist the production of essential war or consumption goods, and to check the growth of mushroom companies. To discourage speculation, all forward and optional dealings in bullion were prohibited. In July, the government assumed powers under the Defence Regulations to prohibit bank advances against any commodity mentioned by them. At last, the occurrence of the Bengal famine forced the hands of the government, which gradually adopted measures to ration the essential commodities in short supply among the urban population. A scheme for the production of "standard cloth" at lower prices was given effect to cope with the problem of the serious rise in cloth prices. Lastly, the Reserve Bank began to sell gold in the market in order to bring down the price of gold and to absorb surplus purchasing power.

These price control measures did not attain much success. Goods were seldom available at controlled prices while black markets flourished in respect of every controlled article. Price control merely resulted in

the disappearance of supplies from the market or to chaos in distribution.

Post-war price movements : A large number of writers predicted that with the end of the war and the consequent decline in defence expenditure and demobilisation would lead to what was called the post-war depression. But contrary to all expectations, prices continued on the whole to rise in the post-war period. This will be evident from Table III, containing the average general index number for all the post-war years.

TABLE III

Average general index number (Average of weeks)

1946-47	1947-48	1948-49	1949-50	1950-51	1951-52	1952-53	1953-54
275·4	308·2	376·2	385·4	409·7	434·6	380·6	397·5

It is evident from this table that prices continued rising till the year 1952-53, when there took place a general fall in prices. But prices steadied soon and increased during the next year. These averages conceal a number of interesting cases which are worth separate study. These are to be studied from Table IV.

TABLE IV

Quarterly General Index of Prices

(August 1939=100)

	1st Quarter (April to June)	2nd Quarter (July to Sept.)	3rd Quarter (Oct. to Dec.)	4th Quarter Jan. to March)	March
1946-47	266·2	270·7	281·3	294·7	292·7
1947-48	296·2	298·6	317·7	349·2	343·6
1948-49	384·8	382·9	382·5	369·8	370·2
1949-50	377·3	388·3	379·0	390·8	392·4
1950-51	397·1	413·8	412·7	449·6	438·6
1951-52	456·9	439·9	435·6	407·9	377·5
1952-53	373·2	386·7	381·2	381·4	385·2
1953-54	395·9	407·3	391·2	395·8	394·0

In about four years, 1946-47 to September, 1949 when devaluation of the rupee was carried, prices no doubt increased on the whole. But

these were at least four different trends during these years. In the first phase, from April, 1946 to November, 1947, prices increased at a comparatively slow rate, the index number rising from 252·7 to 296·7 during this period, *i.e.*, a rise of 44·0 points in 20 months. In the second phase, from November, 1947 to July, 1948, prices jumped up at a faster rate, following the adoption of the policy of decontrol. Thus during these 9 months, prices rose by 92·9 points, *i.e.*, an average of more than 10 points per month as compared to that of a little more than 2 points per month in the first phase. In the third phase, the index number declined from the peak in July, 1948 when it rose to 389·6 to 370·2 in March, 1949. This was due to the re-imposition of controls and to other earnest efforts to bring down prices. But from April, 1949 to August, 1949, prices again resumed an upward trend, rising from 37·2 to 389·8 in August, 1949.

Price movements, 1949-1956 : Price movements since September, 1949, exhibit five distinct trends :—first, the period from September 17, 1949 to April 14, 1951, prices rose almost continuously ; Second, from April 14, 1951 to March 15, 1952—a period of declining prices ; followed by a phase of rising prices from March 15, 1952 to August 13, 1953 ; in the next period until June 14, 1955 prices declined considerably ; and lastly, we come to the present phase,—one of rising prices, which has continued for a long time.

In the first period, starting from September 17, 1949 to April 14, 1951, prices increased on the whole by about 19·4 p.c. in about 19 months. The rate of increase was at first comparatively slow until the outbreak of the Korean episode, after which there took place a precipitate rise in prices. This was due primarily to the impact of the Korean war and the adoption of stock-piling programmes in essential raw materials. The price index of industrial raw materials jumped up from 494·2 in June 24, 1950 to 699·8 in mid-April, 1951.

The second phase began with the decline in price from April, 1951. The rate of decline was at first slow and hesitant. But by January, 1951, the rate of decline gathered momentum and in the next two months, the index number fell by 52·8 points. Compared with the height of the boom in mid-April, 1951, the total fall was 21 p.c. This decline in price was due to the combination of certain international factors with a number of domestic elements. The main factors were the modification of the U.S. stock-piling programme which curtailed the demand for the

essential materials. The world supply position in regard to a number of commodities such as wool, coal, rubber, cotton etc. improved considerably as a result of large production. Both these factors exercised a downward pull on the prices of important commodities. At home, large domestic production of a number of commodities, the raising of the Bank Rate and the adoption of other measures of monetary control from mid-November, 1951, were also responsible for bringing about this fall in prices. Industrial production during this period rose by 12 p.c. and the increase was especially marked in textiles, iron and steel etc. Agricultural production also improved to some extent. To cope with this situation, the government abolished or reduced some export duties for stimulating exports. Domestic controls over certain commodities were also partially relaxed. The result of all these factors was the arrest of the price decline, and from the third week of March, 1952, prices began to recover.

The third phase one of recovery in prices, lasted from March, 1952 to August, 1953, and in a period of about 17 months the general price level rose by 12 p.c. This boom was on the whole of a mild nature. From August, 1953, prices again started to decline a second time in five years, and by June, 1955, the index number fell by about 16 p.c. In certain sectors the decline was so large as to carry prices almost to the levels prevailing in the early years of the war. This was specially the case with the agricultural prices. In this recession the agricultural prices declined by about 30 p.c., while prices of manufactured goods declined by only 2·5 p.c. This was due to the occurrence of bumper crops in two successive seasons on account of favourable weather conditions.

Rise in price during the Second Plan : The trend towards declining prices spent itself out by the middle of June, 1955, and from that time prices have again started their upward course. At the end of December, 1956, the index number of prices registered an increase of 24 p.c. in a period of 18 months,—a rate of increase which was higher than that obtaining in course of the Korean boom. This rising trend has continued in 1957, and by the end of June, 1957, prices rose by about 3 p.c. over the level of December, 1956. The most significant feature of this rising trend is the increase in food prices which rose by 55 p.c. from the level of June, 1955, as compared to the rise of only 28 p.c. in the general index. The rise in manufacturing prices was by

only 6 p.c. during these two years. The price index of rice has risen during this period by more than 61 p.c. The rise in prices upto 1958 may be regarded as consisting primarily of an increase in food prices and in the prices of certain industrial raw materials. Though the rise in prices has been significant and is threatening to assume the character of an inflationary movement, it should be noted that, as compared to the base year, 1952-57, when prices reached some stability and the Korean inflation had spent itself out, the annual rise in prices has been only by 3·2 p.c. on average till the end of March, 1961. On the whole, during the Second Plan period, the index number of wholesale prices rose by 30 p.c. as against a decline by 18 p.c. during the First Plan period.

TABLE V

Index of Prices (1952-53=100)

(Last month)

Year	All commodities	Food articles	Raw materials	Manufactured goods
1954-55	89·6	82·1	94·6	100·1
1955-56	99·2	94·6	110·6	101·6
1956-57	105·1	101·7	116·8	105·4
1957-58	106·1	103·4	112·9	107·4
1958-59	112·1	112·7	115·9	109·5
1959-60	118·6	116·5	132·0	116·0
1960-61	125·7	117·5	159·1	129·4

What are the causes of this persistent rise in food prices ? During these two years, 1955-57, agricultural production has increased to some extent, though it still lags behind the levels reached in the previous bumper seasons. There has no doubt been some rise in food production, though not to the same extent as in 1953-57. The present rise in food prices has taken place in spite of this increased production. The main factor responsible for the present rise in food prices is the increased money incomes consequent on the large-scale development expenditure in the country. The last year of the First Five Year Plan saw a considerable speeding up of the scale of development expenditure, and the Second Five Year Plan was drawn up on an ambitious scale with large-scale recourse to deficit-financing. All this expenditure led to a rise in money incomes. In a poor country like India, a rise in money incomes is likely to be spent mostly on the consumption of food articles. The

demand for food crops has, therefore, outstripped their supply in spite of rising output. It was only natural that food prices would be rising under the impact of these forces. The extent of the rise in food prices was accentuated to some extent as a result of the hoarding of foodgrains by speculators and dealers, helped, no doubt, by the grant of loans and advances by banks.

This threatening situation on the food front has led to a large number of undesirable consequences. The Government has set up a Food Prices Enquiry Committee to examine the situation and suggest measures for arresting the rise in food prices. As it was not possible to raise food production in the short period or to import foodgrains in sufficient amounts for want of foreign exchange, the remedy had to be concerned mostly with the steps for controlling the demand for foodgrains. The fiscal machinery should be geared up to mop up the excess purchasing power in the country. Stricter control should be exercised over the operations of the banking system so that it might not extend too large a proportion of loans against foodgrains.

One noticeable feature of the rise in prices occurring in 1960 was the increase in the prices of industrial raw materials and manufactured goods. Upto 1959 it was food prices which contributed mostly to the rise in general index. But in 1960 the principal feature in the price situation was the sharp rise in the prices of industrial raw materials (16 p.c.) and manufactured goods (10 p.c.) Prices of foodgrains actually declined during this year due to the fall in the prices of rice and wheat.

Price increased during the Third Plan : Over the Third Plan period, the index of general prices rose by 35·2 p.c., *i.e.* an average of more than 7 p.c. per year. It should be remembered that the extent of the rise in price during the previous 5 years was 30 p.c., or 6 p.c. per annum, coming to actual annual rates of change, the price level declined by 3·1 p.c. in the 1st year of the Third Plan. The was, however, offset by the rise that took place in the next year (1962-63) by 3 p.c. But in the succeeding 3 years, prices increased more or less continuously by 9·4 p.c. in 1963-64, 8·8 p.c. in 1964-65 and 13·8 p.c. in 1965-66. What was remarkable was that the rise in prices that took place in 1964-65 occurred in spite of a larger agricultural production during 1964-65 and higher foodgrains imports (the index of agricultural

production rose by 10·5 p.c. during the year). In 1965-66, however, there was a serious shortfall in agricultural production, and the rate of growth in industrial output began to slacken in the second part of the year 1965-66 on account of shortage of raw materials and components. The pressure on prices, coming from these two factors, was further aggravated by the expansionary impact of the large deficits of the Union and State governments. These deficits amounted to Rs. 165 crores and Rs. 189 crores respectively in 1965-66. The situation was further aggravated in 1965-66 by the decline of market arrivals of some cereals like rice in expectation of a serious shortfall in agricultural production in the 65-66 season.

A significant feature of the price trends was the substantial rise in the prices of food articles, industrial raw materials and intermediate products. Prices of food articles rose by 14·2 p.c. in 1963-64, by 8·9 p.c. in 1964-65 and by 14·3 p.c. in 1965-66. Prices rose more in the case of rice which rose by 23·9 p.c., edible oils by 43·5 p.c. There was also a marked rise in the prices of industrial raw materials, which went up by 11·8 p.c. in 1964-65 and by 28·6 p.c. in 1965-66. The increases were most conspicuous in the case of raw jute which rose by 61·8 p.c. and oil seeds by 35·8 p.c. The sharp rise in food prices, industrial raw materials and higher wages as also severe import restrictions led to an increase in the prices of manufactures by 11·4 p.c., in 1965-66 as against 6·3 p.c., in the previous year. The rise was shared by both intermediate products like linseed oil (63·8 p.c.), rayon yarn (33·0 p.c.), metals (18·5 p.c.) and finished products.

The government adopted a number of measures to cope with the situation. These measures aimed at minimising the hardship to low and fixed income groups such as the imposition of statutory rationing in the major cities and increasing the prices of fair price shops. Thus statutory rationing was introduced in towns with a population of one lakh and above, so far it has been introduced in greater Calcutta, Asansol, Durgapur, Siliguri, Delhi, Madras, Coimbatore, Visakhapatnam, Hyderabad, Secunderabad, Kanpur, Bombay, Poona, Nagpur, and Sholapur. Other States have been making preparations for introdu ing it in the major towns. The number of fair price shops were increa ed from 60 thousand at the end of 1963 to 1·11 lakhs at the end of 19 5. At the same time the government made energetic efforts to procure grains from the internal markets. In 1965-66 rice was procured largely

by means of a levy on rice-millers and dealers. In 1965-66 most of the States resorted to procuring paddy from the cultivators. In Madras, Mysore, Kerala, West Bengal, Madhya Pradesh and Bihar, paddy is being procured by a system of levy on an acreage basis. Assam, Orissa and Maharashtra have introduced monopoly procurement system.

Other measures have been adopted to encourage the production of foodgrains. The government fixed minimum support price for certain kharif cereals. An Emergency Food Production Drive was undertaken comprising of the following measures, *viz.*, introduction of additional crops in selected irrigated areas, promotion of cultivation of subsidiary root crops like potatoes and topioca, preparation of farm manure in compost pits and mobilisation of electric and diesel pumps for using flow and surface water by means of rift irrigation etc. The import of fertilisers as also of foodgrains had been increased despite the foreign exchange shortage. A number of measures were also adopted to increase industrial production, and the budget for 1965-66 provided substantial fiscal incentives to stimulate industrial production, including the grant of tax-credit certificates to industries to the extent of 25 p.c. of the excise duty paid on output which was in excess of the base year production. The next year's budget provided for an increase in the development allowance to the tea industry. While fresh controls were imposed on a number of industries, these were relaxed in other cases, such as cement, certain categories of imported steel. To boost fertilisers output the government also decided to decontrol for the next 7 years the price, sale and distribution of fertilisers. Simultaneously, suitable monetary measures were adopted to restrain the growth of inflationary pressures.

All these measures did not of course prove very much of a success, as prices continued rising until on June 5, 1966, the government was forced to devalue the rupee by 36·6 p.c. in order to bring the external value of the rupee into better equilibrium with its internal value. To prevent further rise in prices, the government has decided to start a chain of consumers' co-operative stores including co-operative supermarkets for the supply of essential articles to the consumers. There is still a very serious need for a well-thought out price policy to prevent further increases its prices. For, if prices go on rising after devaluation, there will be no escape from further devaluations including other serious steps like the cancellation of currency etc.

A proper price policy is, therefore, an extremely complex affair. Prices, incomes and costs are so inter-related that a careful handling of the situation calls for a skilled balancing of so many conflicting claims. Implementation of such a price policy must also embrace such devices, besides fiscal and monetary control, as price control, zonal arrangements, fixation of the maximum and the minimum prices in certain cases, and a vigorous pursuit of neutralising operations.

Questions

1. Discuss the causes and effects of wartime inflation in India.

2. Explain the reasons for the continued rise of prices in India after the World War II.

3. Account for the sharp rise in the Indian price level from June, 1950.

4. Discuss carefully the various factors which were responsible for the steep decline of prices in India in February, March, 1952.

5. "Commodity prices in India have exhibited three main features over the two years, 1950-51." Discuss this statement.

6. Give a critical account of the monetary and fiscal measures which the government have adopted to fight the inflation.

CHAPTER 39

DISTRIBUTION OF SOURCES OF REVENUE

Distribution under the constitution : The Indian Union has a semi-federal constitution under which a central government and a number of State governments exercise authority over their respective jurisdictions. Since the State governments have been granted autonomy from the control of the Central Government, an attempt has been made in the constitution to endow each government with a definite sum of revenue. Political autonomy implies financial autonomy. The scheme of the division of resources in the Indian constitution has, therefore, tried to make a distinction between the taxes to be levied by the Central and the State governments. In general, these taxes that have an inter-State base have been left to the legislative jurisdiction of the Central Government, though it does not indicate that the yield will be enjoyed only by the Central Government. On the other hand, those taxes that have a local base have been placed under the legislative jurisdiction of the States. An attempt has been made to frame a comprehensive enumeration of taxes, and each tax has been placed under either the Central or the State Government. There is no overlapping jurisdiction, and little scope for the competitive exploitation of the same tax by different sets of government.

If we examine the scheme of division of resources adopted in the Indian constitution, we shall find that certain taxes have been allocated exclusively either to the Central or to the State Government. Secondly, there are a number of taxes which will be levied by the Centre which may share the proceeds with the State Governments. Thirdly, there are others the proceeds of which, though levied and collected by the Centre, would be handed over entirely to the State Governments. Lastly, income tax has been placed in a special category to be shared by the governments according to pre-arranged percentages.

Thus the State Governments have been given exclusive jurisdiction to levy and collect the following sources of revenues *viz.*, land revenue, taxes on land and building and mineral rights, taxes on agricultural land, excise duties on drugs, narcotics and alcoholic liquors, taxes on luxuries including taxes on entertainments, amusements, betting and gambling, sales taxes, taxes on professions, trades, callings and employ-

ments, etc. Secondly, with regard to certain other taxes, the States are to enjoy the whole of their proceeds, but these are to be levied by the Central Government. These are estate and succession duties on property (other than agricultural land), terminal taxes on goods and passengers carried by railways, taxes other than stamp duties on transactions in stock exchanges and futures markets, and taxes on the sale or purchase of newspapers and on advertisements published therein. Thirdly, certain taxes like stamp duties and excise duties on medicinal and toilet preparations containing alcohol or opium or other drugs are to be levied by the Central Government. But they are collected by the State Governments which enjoy the whole of their revenues.

Similarly, the Central Government has been given the exclusive right to levy and enjoy the proceeds of the following taxes, *viz.*, corporation tax, customs duties, taxes on the capital value of assets (exclusive of agricultural land), taxes on individual and companies, surcharge in certain other taxes like the estate and succession duties etc.; the incomes from railways, posts and telegraphs, currency and mint etc.

Thirdly, duties of excise on commodities are to be levied and collected by the Central Government, which may, however, hand over a part or the whole of the proceeds of any such excise duty to the State Governments.

Lastly, as regard income tax which is to be levied and collected by the Central Government, the Central Government will retain (*i*) the proceeds of this tax on federal emoluments, (*ii*) the surcharge on income tax, of levied, and (*iii*) a certain percentage of the proceeds of the personal income tax. The rest is to be handed over and distributed among the States. The percentage of the proceeds of this tax to be handed over to the States is to be determined by the President from time to time on the recommendation of the Finance Commission to be set up by him.

This is, in short, the scheme of distribution laid down in the present Indian constitution. Though the scheme is, in essentials, the same as that included in the Government of India Act of 1935, there are some differences. In the first place, under the 1935 Act, export duties belonged to the category of taxes to be levied and collected by the Central Government, which might, and must in the case of jute export duties. hand over a part or whole of the proceeds to the State Govern-

ments. In the present constitution export duties are wholly a central source of revenue, just like the import duties.

But the Central Government has been required to pay grants-in-aid to the jute-growing States in lieu of their share of the proceeds of the jute export duty. Secondly, greater flexibility had been introduced with regard to the sharing of the proceeds of the income tax between the centre and the States in the Indian constitution than was the case in the 1935 Act. Thirdly, the present constitution incorporates certain restrictions on the powers of State to levy sales taxes. States are prohibited from imposing any such taxes on commodities whose sale or purchase take place outside the jurisdiction of the States and on commodities declared by the Parliament to be essential to the life of the community. These restrictions were not to be found in the 1935 Act.

There is no ideal system of distribution of sources of revenue between the federal and State Governments. The division in most federations has been based, more or less, on historical reasons, and expediency, rather than any desire to adhere to strict scientific principles. The division of sources in the Indian constitution is no exception. There is, for example, no justification for treating agricultural income separately from other incomes for purposes of income taxation, except perhaps historical reasons. When income tax was first levied in India, agricultural income was excluded from this tax in the mistaken belief that the Permanent Settlement Regulations stood in the way of the imposition of an income tax on such incomes. Though there was no legal or constitutional basis for such a belief, the exclusion still now remains a part of the Indian constitution. Similarly, it is difficult to see any justification for the provision which lays down that while the estate duty on all other forms of property is to be levied and collected by the Central Government, that on agricultural land is to be levied and collected by the State Governments.

The greater flexibility with regard to the distribution of income tax is of course a great merit of the scheme laid down in the present constitution. But the determination of the actual percentage of income tax to be distributed among the States at the end of every five years may give rise to much bickerings among the states at the time of each settlement, and States may deliberately follow a policy of manipulating their budgets in such a way as to have a perpetual deficit for the sake of

strengthening their case for a larger percentage. The danger is real, and should be guarded against at the time of each re-settlement.

The working of these arrangements since the adoption of this constitution has shown that, faced with comparatively inelastic sources of revenue, the State Governments have come to rely to a large extent on the sales taxes as a means of raising increasing amounts of revenue. This has given rise to a number of difficulties. The multiplicity of rules and regulations framed by different State Governments under the Sales Tax Acts has created immense problems for inter-State trading.

Evolution of the present system : As we have stated in the earlier section, in every federation, the system of distribution of the sources of revenue is usually a mattter of historical conditions. In this section we propose, therefore, to trace the evolution of the system as adopted in the present constitution.

The Charter Act of 1833 centralised sources of revenue in the hands of the Government of India, and the Provincial Governments spent what was given to them by the Government of India. This naturally led to great difficulties as it was nobody's interest among the Provincial Governments to avoid waste and to practise economy. So a process of decentralisation began from 1871, when Lord Mayo transferred certain departments with their revenues to the Provincial Governments, together with fixed lump-sum grants. The next step was taken in 1877, when besides the fixed annual grants, the provinces were assigned certain sources of revenue. From 1882 to 1907 there was a certain division of sources of revenue, kept valid for five years, at the end of which it was revised. These five yearly settlements proved to be a fertile cause of friction, improvidence and waste. So in 1911 the financial settlement was made permanent. The Central Government enjoyed the revenue from customs. salt, opium, posts and telegraphs, mint and state railways, while land revenue, irrigation, excise duties, stamp duties forests and assessed taxes were divided heads of revenue, whose proceeds were shared between the Central and the Provincial Governments.

The Meston Settlement : The Reforms Act of 1919 marked the beginning of a federation in India. Under a mistaken belief that Provincial autonomy implied a complete separation of the sources of revenue of the two sets of government, the Act laid down a scheme of division of sources of revenue. As the scheme was finalised after

an enquiry by a Committee it came to be known as the *Meston Settlement* after the Chairman of that Committee.

Under this Act, the Centre was given the following sources of revenue, *viz.*, customs, salt, opium, income tax, railways, posts & telegraphs, currency and mint and tributes from the Native States. The Provinces collected the following sources of revenue,—land revenue, irrigation, forests, registration, stamps, excise duties on drugs, narcotics etc., taxes on succession, tobacco, amusements etc. They were also to be given a share of the income tax equal to three pies on every additional rupee assessed in 1920-21. As this distribution left the Central Government with some deficits the Provinces were called upon to contribute the sum of Rs. 983 lakhs to the centre.

The greatest defect of this system was that while it gave important sources of revenue to the Centre, the provinces were left with inelastic sources. At the same time they were required to spend money on nation-building developments. Moreover, the provincial contributions were a frequent sources of jealousy between the provinces.

The scheme of distribution under the 1935 Act: The next step was taken in 1935 under the Government of India Act. After a number of enquiries by various Committees, that Act finally included the following scheme of distribution.

The Centre was given the right to levy, collect and spend the whole of the revenues from these sources, *viz.*, import duties, railway, posts & telegraphs, currency and mint, profits from the Reserve Bank and the Corporation tax. Secondly, the Central Government levied, and collected the following sources of revenue,—salt duty, excise duties except on drugs, narcotics etc., export duties. But a part or the whole of the proceeds of any of these taxes might be handed over to the Provinces. In the case of the export duty on jute goods, the Centre must pay 62½ p.c. to the jute-growing Provinces. Thirdly, the Central Government levied and collected stamp duties, terminal taxes on goods and passengers carried by railways, duties on succession to property other than agricultural land. But the whole of the proceeds of these taxes, after deducting the cost of collection, were to be handed over to the Provinces. Fourthly, as regards income tax, the Centre levied and collected it and retained the revenue obtained from centrally administered areas, and a certain proportion of the yield of the tax from other areas. Under the Niemeyer

Award, the proportion was fixed as follows :—if the proceeds of the income tax together with the net revenue from the railways exceeded Rs. 13 crores in any year, 50 p.c. of such excess over Rs. 13 crores was to be handed over to the Provinces. The Central Government was to retain the yield from any surcharge on income tax if and when levied. Lastly, the Provinces would levy, collect and spend the revenues from land revenue, irrigation, forests, registration, excise duties on drugs, narcotics and alcoholic liquors etc., stamps, taxes on agricultural income, taxes on luxuries, entertainment, betting etc.; sales taxes, duties on succession to agricultural land. In addition, certain Provinces received grants in-aid from the Centre.

Niemeyer Award : Before the Government of India Act of 1935 was put into operation, a financial enquiry was held by Sir Otta Niemeyer to determine the financial adjustments necessary for enabling the Provinces to start with reasonable working surplus. His recommendations, later known as the Niemeyer Award, were later incorporated in the Government of India Act of 1935.

As regards the percentage of income tax to be given to the Provinces, he expressed the opinion that for the next 10 years it was not possible for the Centre to hand over 50 p.c. of the proceeds of this tax to the Provinces. So he laid down that the Central Government would retain, out of the proceeds of the income tax collected from the Provinces, a sum, which, together with the net contributions from railways, amounted to Rs. 13 crores, 50 per cent of the excess over Rs. 13 crores would be handed over to the Provinces in the following proportions, *i.e.*, Bengal and Bombay 20 p.c. each, U.P. and Madras 15 p.c. each, Bihar 10 p.c., Punjab 8 p.c., Madhya Pradesh 5 p.c., Assam and Orissa 2 p.c., each. In addition, the jute-growing Provinces were to be given 62½ p.c. of the proceeds of the Jute Export Duty, instead of 50 p.c. The following Provinces were to be granted cash contributions by the Centre at rates mentioned within brackets,—Assam (Rs. 30 lakhs), Orissa (Rs. 40 lakhs), U.P. (Rs. 25 lakhs), Orissa was to get a further non-recurring grant of Rs. 19 lakhs.

This award did not satisfy some of the Provinces. In 1940, as the railways began to yield large surpluses, it was modified by an Order-in-Council, under which the net contributions from the railways were not to be taken into account in determining the share of the

Provinces. For the next three years, the Central Government would retain 50 p.c. of the proceeds of the income tax *plus* an additional sum of Rs. 4½ crores.

Deshmukh Award : The partition of the country in 1947 necessitated some adjustments in the scheme of distribution as at least two Provinces, (Bengal and the Punjab) were divided. The Government of India asked Shri Chintamani Deshmukh to consider the modifications necessary in the scheme of distribution of income tax and Jute Export Duty. Shri Deshmukh was given the duty of determining the shares of Bengal, Assam and the Punjab as these had lost some of their territories to Pakistan, and to re-allocate the surplus among other Provinces. He recommended the following scheme of distribution of the Provincial share of the income tax.

TABLE I

Provinces	*Share before award*	*Share after award*
Bombay	20 p.c.	21 p.c.
Madras	15 p.c.	17·5 p.c.
U. P.	15 p.c.	18 p.c.
West Bengal	12·5 p.c.	13·5 p.c.
Bihar	10 p.c.	12·5 p.c.
C. P. & Berar ..	5 p.c.	6 p.c.
East Bengal	4 p.c.	5·5 p.c.
Orissa	3 p.c.	3 p.c.
Assam	3 p.c.	3 p.c.

As regards the allocation of Jute Export Duty, he recommended that West Bengal was to get Rs. 105 lakhs, Assam Rs. 40 lakhs, Bihar Rs. 35 lakhs and Orissa Rs. 5 lakhs.

As usual, no award could satisfy all the States. But Shri Deshmukh's task was a very limited one of securing a proper distribution of the additional funds which became available with the partition of the country. He did not conceive it to be his business to start new allocation of the sources of revenue. That was naturally left by him to the framers of the new constitution that was being prepared.

Finance Commissions : The Indian Constitution provided for the setting up of a Finance Commission by the President with 2 year's

from the commencement of the constitution and thereafter at the end of every fifth year, or earlier, if necessary. The first Finance Commission was appointed in 1951 under the chairmanship of Shri K. C. Neogy to consider (*a*) the distribution between the Union and the States of the net proceeds of taxes which are to be or may be divided between them and the allocation between the States of the respective shares of such proceeds, (*b*) the principles which should govern the grants-in-aid of the revenues of the States out of the Consolidated Fund of India and any other matter referred by the President in the interests of sound finance. The Commission submitted its report in 1952 and its recommendations have been accepted in toto by the Government, thus establishing a valuable precedent.

According to the Commission, the approach to the problem of federal finance should be governed by the consideration that in the scheme of distribution of revenues not merely the growing needs of the States for more revenue but also the capacity of the Centre to transfer resources should be taken into account. For it is unnecesssary for us to emphasize that the prosperity of the States must rest on the solid foundation of a reasonably strong and financially stable centre." At the same time the scheme must also seek to bring about relative degrees of equality in the standard of administration and welfare among the different States. So the Commission kept three considerations in view :—

"Firstly, the additional transfer of resources from the centre must be such as the centre could bear without undue strain on its resources, taking into account its responsibility for such vital matters as the defence of the country and the stability of its economy.

Secondly, the principles for the distribution of revenues between the States and the determination of the grants-in-aid must be uniformly applied to all the States.

Lastly, the scheme of distribution should attempt to lessen the inequalities between States."

In recommending the transfer of resources from the Centre to the States the Commission suggested both the methods of devaluation of revenue and grants-in-aid, but relied mainly on the former. For this purpose it recommended not only an increase in the share of the income

tax to be distributed, but also provided for the distribution of a few excise duties.

As regards the *distribution of the income tax* the Commission recommended an increase in the states' share from 50 to 55 per cent., in order to meet the almost unanimous demand of the States, and in view of the fact that there would now be 16 participants in the States' share of the divisible pool as against 9 in the past.

Principles of distribution : Regarding the principles to be followed in distributing the divisible pool among the States, the Commission mentioned seven principles, *viz.*, (i) the collection of income tax in the States, (ii) the amount of income tax realised in respect of incomes, wherever earned, of individuals resident in the different States, (iii) the collection of income tax in different States with reference to the origin of the income, (iv) the relative population of each State, (v) the relative volume of industrial labour in each State, (vi) the relative per capita incomes of the States, and (vii) the needs of each State according to various criteria, *e.g.*, area or sparseness of population, economic backwardness or the inverse, relative *per capita* income of each State.

The first three criteria seek to relate distribution to the respective contributions of the States to the total proceeds. They would naturally favour Bombay and West Bengal, where 39·6 p.c. and 35·8 p.c. respectively of the total income tax were collected in 1950-51. But the collection of the tax is not an adequate index of contribution. The large collections of income tax from Bombay and Calcutta are due to the fact that the head offices of companies operating all over the country are concentrated in these two cities. Thus the Tatas have their head office in Bombay, where they are assessed to income tax, whereas their factories are situated in Bihar, Orissa and other States.

As regards the fifth principle, the Commission did not accept the argument that the number of industrial labour in each State provides some measure of its contribution to the total proceeds and at the same time gives some idea about its needs. A State with a large labour force has to meet additional expenditure in maintaining law and order and in providing amenities for these labourers. In its opinion this principle provides only a partial index of either contribution or needs. The sixth principle, *per capita* income in each State, was dismissed on the ground that figures of *per capita* incomes for individual States were not available.

On the whole, therefore the Commission came to the view that the needs of each State should form the main criteria of distribution. But such needs were best measured broadly by the respective populations of each State. Additional tests of the needs criteria such as sparseness of population, economic backwardness, low *per capita* incomes etc., should be taken into consideration not in the distribution of the income-tax, but in the determination of the grants-in-aid.

While the needs of the State as determined by its population should thus be the main criteria, some weight should also be given to the factor of contribution. "There is all over the country a core of incomes—particularly in the range of personal and small business incomes—which could be treated as of local origin."

Hence the Commission recommended that 80 p.c. of the divisible pool of the income tax should be distributed on the basis of population, 20 p.c. on the basis of the relative collections of the States. Calculating on the basis of these two considerations, the shares of each State would be determined in the following manner. (Table II).

TABLE II

State	Existing per cent	Per cent recommended by the Commission
Assam	23	2·25
Bihar	12·5	9·75
Bombay	21	17·50
Hyderabad		4·50
Madhya Bharat ..		1·75
Madhya Pradesh ..	6	5·25
Madras	17·5	15·25
Mysore		2·25
Orissa		3·50
PEPSU	23	0·75
Punjab	5·5	3·25
Rajasthan		3·50
Saurashtra		1·00
Travancore-Cochin ..		2·50
Uttar Pradesh	18	15·75
West Bengal	13·5	11·25
Part C States	1	2·75

The Commission next recommended the distribution of 40 p.c. of the proceeds of the excise duty on tobacco, matches and vegetable ghee among the States in order to augment their resources. Since we do not possess statistics of consumption of these goods in different States, they fell back upon their respective population as the criterion for the distribution of revenues from these sources. So they fixed the following percentages of distribution, *viz.*, Assam 2·6 p.c., Bihar 11·6 p.c., Bombay 10·37 p.c., Hyderabad 5·39 p.c., M.B. 2·29 p.c., M.P. 6·13 p.c., Madras 16·44 p.c., Mysore 2·62 p.c., Orissa 4·22 p.c., Pepsu 1·00 p.c., Punjab 3·66 p.c., Rajasthan 4·41 p.c., Saurashtra 1·19 p.c., Travancore-Cochin 2·68 p.c., U.P. 18·23 p.c., and West Bengal 7·16 p.c.

With regard to the amounts of grants-in-aid in lieu of the Jute Export Duty, the Commission recommended that the *pro rata* share of the jute-growing States in the divisible pool should be on the following basis :—West Bengal Rs. 150 lakhs, Bihar Rs. 75 lakhs, Assam Rs. 75 lakhs and Orissa Rs. 15 lakhs.

After discussing the principles for the distribution of the grants-in-aid the Commission recommended grants-in-aid of Rs. 80 lakhs to West Bengal to enable it to meet the special problems created by the partition, Rs. 75 lakhs to Orissa as it had large backward tracts and population, Rs. 40 lakhs for Saurashtra, Rs. 125 lakhs for Punjab, as it had additional responsibilities for maintaining law and order ; Rs. 1 crore to Assam, Rs. 40 lakhs to Mysore and Rs. 45 lakhs to Travancore-Cochin. Besides these general grants, special grants have been recommended to some States for the purpose of expanding primary education to the level of other States.

For purposes of comparison the Commission have calculated a table showing the total amounts which the States receive or would receive from the Centre under various items during 2 or 3 years ending 1951-52 and under their recommendations.

TABLE III

States	Total received on average during 1949-50 to 1951-52	Total receivable under Commission's award
Assam	Rs. 221 lakhs	Rs. 345 lakhs
Bihar	Rs. 655 "	Rs. 855 "
Bombay	Rs. 1,160 "	Rs. 1,125 "
Hyderabad	Rs. 125 "	Rs. 359 "
M. B.	Rs. 6 "	Rs. 146 "
M. P.	Rs. 335 "	Rs. 420 "
Madras	Rs. 856 "	Rs. 1,110 "
Mysore	Rs. 345 "	Rs. 368 "
Orissa	Rs. 201 "	Rs. 374 "
PEPSU	Rs. 16 "	Rs. 65 "
Punjab	Rs. 343 "	Rs. 382 "
Rajasthan	Rs. 10 "	Rs. 289 "
Saurashtra	Rs. 275 "	Rs. 302 "
Travancore-Cochin	Rs. 322 "	Rs. 323 "
U. P.	Rs. 888 "	Rs. 1,170 "
West Bengal	Rs. 754 "	Rs. 960 "

An examination of the principles of distribution : The Commission have relied mainly on the population criterion and to some extent on collections in devising a scheme for the distribution of the divisible pool of income-tax. They have assumed that the needs of a State would be best measured by its population, while other tests of need like area or sparseness of population, economic backwardness, financial difficulties, special burdens or commitments of a State etc., should be taken into account of in the distribution of grants-in-aid. Again in the distribution of the proceeds of the excise duties they have relied solely on the population of the States. So there are two assumptions. The more is the population of a State the more is its need for revenue, and the more is its *per capita* consumption to tobacco, matches and vegetable ghee. Both these assumptions are highly questionable. Population is not a satisfactory test of need. To distribute revenues on the basis of population means the payment of equal *per capita* shares to the poor as well as to the rich States. The *per capita* needs of a comparatively rich State like Bombay

cannot be equal to those of a poor State like Orissa or Assam. Justice requires that more revenues should be distributed to the poor but sparsely populated States than to a rich and highly populated State. So other considerations like the *per capita* income on a State and the sparseness or otherwise of its population must be taken into account in securing an equitable distribution of revenues. Unfortunately the Commission have not taken these factors into consideration, even in the distribution of grants-in-aid.

Nor does mere population provide a good test for distributing the revenue from the excise duties. *Per capita* consumption of these commodities is not necessarily higher in a populous State than that in a sparsely populated State. Here also *per capita* incomes and other factors would probably provide a better test of consumption than that adopted by the Commission. Population would be a good test, both of needs and of consumption, only if the economic conditions are nearly similar in different States. Where they differ, the test of population must prove inadequate and inequitable.

Hence regard must be paid to other factors. Collection does not, of course, provide a satisfactory test of needs. But the question may be asked, why should not a State be allowed to get the benefit, or at least some benefit, from the enterprise of its citizens who have borne considerable risks in setting up industrial concerns ?

In fact, no such simple formula like mere population *plus* collection would ensure an equitable distribution of revenues among the different States. Regard must also be paid to other factors like the *per capita* income, the sparseness or otherwise of the population and the history of the growth of its various administrative services in the past etc. A sparsely populated State may have been forced to spend comparatively less on its administration either because of its poverty or because of the neglect of the central government in the past. It must now have larger *per capita* revenue if it is to bring its administrative services upto the level of other more fortunate States. But the population-cum-collection formula would not provide it with the needed revenue.

The Second Finance Commission : The Indian Constitution provides for the setting up of a Finance Commission by the President at the end of every five years to make recommendations for the distribution of the proceeds of the income tax and other central taxes among

the States. The recommendations of the first Finance Commission have already been reviewed. The Second Finance Commission was set up in 1956 and submitted its report with its recommendations. These have been accepted by the government and placed before the Parliament on November 14, 1957.

The Commission had to determine the distribution of four different taxes, income tax, excise duties, estate duty and the tax on railway passengers. In addition, it had to decide the principles and the amount of grants-in-aid to the States from the Centre. As regards income tax, it has recommended that 60 p.c. of the proceeds of the personal income tax (excluding the surcharges) is to be distributed among the States according to the following proportions :—

TABLE IV

Share of the Income tax

Andhra Pradesh ..	8·12 p.c.	Orissa ..	3·73 p.c.
Assam ..	2·44 „	Punjab ..	4·24 „
Bihar ..	9·94 „	Rajasthan ..	4·09 „
Bombay ..	15·99 „	U. P. ..	16·36 „
Kerala ..	3·64 „	W. Bengal ..	10·08 „
Madhya Pradesh	6·72 „	Jammu & Kashmir ..	1·13 „
Madras ..	8·40 „		
Mysore ..	5·14 „		

The Commission has followed population as the basis of distribution. With regard to the estate duty, it has recommended that 1 p.c. of the net proceeds of this duty should be retained by the Centre as proceeds attributable to the Union Territories. The balance is to be divided into two parts,—the proceeds attributable to immovable property and to other property. This is to be done on the basis of the gross value of all such properties brought into assessment in any year. The part of the duty attributable to immovable property is to be paid to the States in proportion to the gross value of the immovable property located in each State. The second part,—proceeds of the duty on other properties—is to be distributed among the States in proportion to their population.

As regards Union excise duties, the first Finance Commission provided for the distribution of 40 p.c. of the proceeds of such duties on tobacco, matches and vegetable ghee among the States. The Second Commission has lowered the ratio to 25 p.c., but has recommended the inclusion of the proceeds of more excise duties in the divisible pool. As a result, it is expected that a larger share of such duties than at present would be available for distribution. As distribution on the basis of population only would place a few States into a favourable position, the Commission decided that while 90 p.c. of the States' share of the divisible Union excise duties should be distributed on the basis of population, the remaining 10 p.c. was to be used for making suitable adjustments. Population is also the main factor for the distribution of the proceeds of the tax on railway fares levied in the budget of 1957-58.

TABLE V

States' shares in Union excise duties, estate duty and tax on railway fares.

	Share of Estate Duty	Share of Union Excise Duties	Share of the tax on railway fares
Andhra Pradesh ..	8·76 p.c.	9·38 p.c.	8·86 p.c.
Assam ..	2·53 ,,	3·46 ,,	2·71 ,,
Bihar ..	10·86 ,,	10·57 ,,	9·39 ,,
Bombay ..	13·52 ,,	12·17 ,,	16·28 ,,
Kerala ..	3·79 ,,	3·14 ,,	1·81 ,,
M. P. ..	7·30 ,,	7·46 ,,	8·31 ,,
Madras ..	8·40 ,,	7·56 ,,	6·46 ,,
Mysore ..	5·43 ,,	6·52 ,,	4·45 ,,
Orissa ..	4·10 ,,	4·16 ,,	1·78 ,,
Punjab ..	4·52 ,,	4·50 ,,	8·11 ,,
Rajasthan ..	4·47 ,,	4·71 ,,	6·77 ,,
U. P. ..	17·71 ,,	15·94 ,,	18·76 ,,
W. Bengal ..	7·37 ,,	7·59 ,,	6·31 ,,
Jammu & Kashmir ..	1·24 ,,	1·75 ,,	

The last question to be considered was the distribution of grants-in-aid to the States. Under the present constitution, the grants-in-aid in lieu of the jute export duty paid to the jute-growing States are to cease at the end of 1959-60. The West Bengal Government asked that this should be made permanent. This was not accepted

by the Commission, which recommended that these grants were to continue for the next 3 years only. Regarding general grants-in-aid, the Commission examined the peculiar needs and problems of every State. Bombay, Madras and U.P. do not have deficit budgets, and will not be given any grants-in-aid. It recognised the special problems of West Bengal, caused by the influx of refugees, and so recommended a grant of Rs. 3·25 crores. The amount is to be raised to Rs. 4·75 crores in 1960-61 and 1961-62 to compensate that State temporarily for the cesation of the grants-in-aid in lieu of jute export duty from 1959-60. Similarly, Bihar which will normally receive a grant-in-aid of Rs. 3·50 crores will be paid Rs. 4·25 crores in these two years. Assam's grant-in-aid of Rs. 3·75 crores would also be raised to Rs. 4·50 crores and that of Orissa from 3·25 crores to Rs. 3·50 crores for these two years.

The Commission have also made a number of recommendation for securing the repayment of all central government loans to the States.

The adoption of population as the basis of distribution is certainly defective from many points of view. The administrative needs of a thickly populated region may not be definitely larger than those of another State which is sparsely populated over a larger area. All these arguments aginst the population basis have been examined in detail in another part of this book. There is no necessity to repeat them at this place. The argument of this Finance Commission that the urbanised, industrial States have other sources to raise large revenues, and so have no special claim in regard to the distribution of the proceeds of the income tax and the excise duties is clearly beside the point. Both U. P. and Bihar also derive large yields from land revenue, and so do not deserve any special consideration at the cost of the industrial States. While the industrial States have no doubt benefitted through the utilisation of such sources of revenue as motor vehicles tax, sales tax, electricity duties, entertainment taxes etc., the so-called rural States have also been benefitted considerably through the abolition of zemindari estates, sugarcane cesses etc., There is no doubt that some injustice has been done to the industrial States in the new scheme of distribution of revenues.

The Third Finance Commission : The Third Finance Commission was set up in December, 1960 and issued its report in December, 1961. Its report was unanimous except in respect to two recommendations. All the unanimous recommendations have been

accepted by the government, which has also accepted only one of the disputed recommendations of the **majority.**

The Commission recommended that in view of the shrinkage of the divisible pool as a result of the exclusion of the income tax paid by companies from the pool, the States' share in the personal income tax be raised from 60 p.c. to 61·66 p.c., while the share of the union territories be also raised from 1 p.c. to 2·5 p.c. As regards the distribution of this total among the individual States, the Commission was of the opinion that, while population should remain as the main factor, the factor of contribution should now be given greater weight than had been done by the Second Finance Comission. Now that the tax paid by the companies had been excluded from the pool, the remaining portion of the divisible pool could now be said to be derived from incomes of local origin. Hence origin or the place of collection should be given greater weight than had been the case before. Secondly, the industrial States had to spend more money on the provision of administrative and social services than was the case with the other States. So the Commission recommended the distribution of the divisible pool of income tax among the individual States on the basis of 80 p.c. for population and 20 p.c. for collection. So the shares of the States would be like the following table :—

TABLE VI

12% shares of States

Andhra Pradesh	..	..	7·71%
Assam	..	..	2·44 ,,
Bihar	..	..	9·33 ,,
Gujarat	..	..	4·78 ,,
J. & K.	..	..	0·70 ,,
Kerala	..	..	3·55 ,,
M. P.	..	..	6·41 ,,
Madras	..	..	8·13 ,,
Maharashtra	..	..	13·41 ,,
Mysore	..	..	5·13 ,,
Orissa	..	..	3·44 ,,
Punjab	..	..	4·49 ,,
Rajasthan	..	..	3·97 ,,
U. P.	..	..	14·42 ,,
W. Bengal	..	..	12·09 ,,

As regards excise duties, the Commission recommended that, in view of the need for additional revenues for the States, the number of excisable commodities in the divisible pool should be increased from 8 to 35 by including all commodities on which excise duties were levied in 1960-61. At the same time the States' share of the divisible pool was reduced from 25 p.c. to 20 p.c., and in determining the relative shares of each State, while population should be continued as the major factor, other elements as the relative financial weakness of the State, the disparity in the levels of development reached by it, the percentage of scheduled castes and tribes and backward classes in the population of the State etc. should also be given some weight.

As regards the distribution of additional excise duties on mill-made textiles, sugar and tobacco, levied in lieu of the sales tax, the Commission recommended that, after meeting the guaranteed amount, excess collections are to be distributed partly on the basis of the percentage increase in the collection of sales tax in each State after 1957-58, and partly on the basis of collections. With regard to grants-in-aid, the Commission have recommended an annual payment of a total sum of Rs. 110·25 crores to all States except Maharashtra. Of this amount Rs. 52 crores are for filling the revenue gap, and the balance for meeting 75 p.c. of the revenue component of the States' plans. In making the last recommendation the Commission took an integrated view of the entire revenue budget of a State. Finally, the Commission have recommended that during the 4 years, 1962-66, a sum of Rs. 36 crores (or Rs. 9 crores a year), being approximately 20 p.c. of the proceeds of the duty on motor spirits, should be distributed among the States as a special purpose grant for improvement of communications.

One of the most interesting recommendations of this Commission relates to the setting up of an independent Commission to examine such important questions as the assessment of the tax potential of each State, review of its tax structure, of and the fixation of rates under different heads of levies in the State List. This Commission was also to examine the widening gap between the resources and functions of the States brought about mainly by the planning process and to consider what adjustments were to be made in the financial relations of the Union and the States so as to strengthen the position of both.

TABLE VII

		Share of Union excise Duties	Share of Estate Duty
Andhra Pradesh	..	8·23%	8·34%
Assam	..	4·73 „	2·75 „
Bihar	..	11·56 „	10·78 „
Gujarat	..	6·45 „	4·78 „
J. & K.	..	2·02 „	0·83 „
Kerala	..	5·46 „	3·92 „
M. P.	..	8·46 „	7·51 „
Madras	..	6·08 „	7·80 „
Maharashtra	..	5·73 „	9·16 „
Mysore	..	5·82 „	5·46 „
Orissa	..	7·07 „	4·08 „
Punjab	..	6·71 „	4·71 „
Rajasthan	..	5·93 „	4·67 „
U. P.	..	10·68 „	17·10 „
W. B.	..	5·07 „	8·10 „

Grants-in-aid : The system of grants-in-aid implies that the federal government hands over a certain portion of its revenue to some State Governments or to all State Governments as a general aid or to compensate them for loss of revenue resulting from the federalisation of certain taxes previously levied by these States. Instances of grants-in-aid made from both these motives are to be found in the Indian constitution. Thus the grants-in-aid in lieu of the Jute Export Duty provides an instance of the second type of grants while instances of grants-in-aid made for general purposes are to be found in the Grow-More-Food Scheme grants, development grants etc.

This mode of distribution of federal revenues among the States can be found in almost every federation. It is a method whereby the federal government can make up deficiencies in some States and thus overcome state-federal disequilibrium of resources resulting from the constitutional arrangements. Such grants may be unconditional or conditional. In unconditional grants, money is given for general aid, and no strings are attached as to the manner in which they are to be spent. Conditional grants are those given for specific purposes, such

as the grants awarded by the Finance Commission to some States for the expansion of primary education.

The Finance Commission has discussed several principles for distributing the grants-in-aid ;—budgetary needs, tax effect, economy in expenditure, standard of social services, special obligations and broad purposes of national importance.

The Commission considered that budgetary needs were an important criterion for determining whether and to what extent, a State was in need of funds. The budget has necessarily to be the starting point of an examination of fiscal need. But in order that the budgets of different States may be in a comparable position, certain adjustments in respect of any abnormal or unusual and non-recurring items of receipts or expenditure would have to be made.

The second criterion is the *tax effort* put forth by the State Government to meet its needs. A State which has already raised the maximum revenue through taxation has a better claim for federal aid than another which has not utilised all its scope for additional taxation. Moreover, if a State which has not made the maximum tax effort is granted federal aid, such assistance may go to relieve those who are comparatively well off from the necessity of contributing more to the State revenues rather than help to increase public expenditure for the benefit of the poorer sections of the people.

Just as a State making the maximum tax effort is entitled to our consideration, so also does a State which has practised economy in its public expenditure. If this is not done, then a direct premium might be placed on impecunious policies and a penalty imposed on financial prudence.

The fourth criterion is the standard of social services in a State. This is important as the general purpose of the system of grants-in-aid is to help in equalising standards of social services in different States.

Grants-in-aid may also be given to enable a State to meet some special burdens or obligations like those left by the partition of the country. Lastly, grants-in-aid may be given to further any beneficient service of primary importance in respect of which it is in the national interest to assist the less advanced States.

The most serious criticism that has been brought against this principles. They laid primary emphasis on the budgetary needs of a

State, and took into account any additional burdens it had to bear due to the partition, and lastly, the need for assisting the less developed States to raise the standards of one of the important social services.

It is important to note that the principles according to which grants-in-aid are to be distributed must be definite and precise in order to avoid inter-State jealousies and political bargaining. At the same time they must ensure that greater aid goes to the more needy States. Any particular criterion by itself may not prove adequate. The Nehru-Adarkar report has stated that "in the allocation of grants......the fullest consideration will have to be given to all relevant factors, including the size of the population, the wealth of natural resources, the existing backwardness of the areas concerned, the geographical density of population, the *per capita* income and wealth of the peoples of the provinces and their basic needs." But to take account of so many factors in the distribution of grants in a satisfactory manner may not be a practicable proposition. The best as well as the simplest criterion is the *per capita* income in a State, allowance being made for the sparseness or otherwise of the population. But unfortunately it is only in recent years or so that a few States have taken steps to collect figures of their *per capita* incomes.

Present distribution of revenue between the Centre and the States : After the incorporation of the recommendations of the Finance Commission of 1961, the distribution of revenue between the Centre and the States is as follows :

The Central Government levies, collects and enjoys the revenue from the customs, proceeds of the union excise duties with the exception of 20 p.c. of the excise duty on all articles, posts and telegraphs, railways, currency and mint, profits from the Reserve Bank etc.

The State Governments levy, collect and enjoy the revenue from land revenue, fisheries, irrigation, forests, registration, court fees, sales tax, taxes on entertainments, amusements, betting and gambling, tax on electricity, agricultural income tax, etc. It may levy duties on succession to agricultural land.

The Central Government levies, collects, but hands over the entire proceeds (excepting cost of collection), of estate and succession duties, stamp duties, terminal taxes on goods and passengers carried by railways,

The Central Government levies and collects the income tax including the corporation tax. It retains the entire proceeds of the Corporation tax, and of the tax collected on the incomes of federal officers, plus 25 p.c. of the proceeds of the personal income tax. The remaining 75 p.c. is distributed among the States according to certain fixed proportions.

The Fourth Finance Commission : This Commission was set up in May 1964 and submitted its report in August, 1965. It was given much wider terms of reference, such as the consideration of the combined incidence of union excise duties and sales taxes on production, consumption and export of articles. Its major recommendations are the following :—

With regard to income tax, the Commission decided that 75 p.c., instead of $66^2/_3$ p.c., of the divisible pool of income tax should be assigned to the States for distribution among them. Regarding the determination of the States' share in the divisible pool, it recommended that the only relevant factors to be taken into consideration were contribution and population. Feeling that some amount of certainty and stability should be imparted to the principles of distribution, it recommended a reversion back to the proportions contained in the reports of the 1st and the 2nd Finance Commissions, *i.e.*, 80 p.c. on account of population and 20 p.c. on account of collection. The share of the Union Territories in the divisible pool of income tax was to be fixed at 2·5 p.c.

As regards union excise duties, the Commission recommended that excise duties levied on all commodities excepting certain special excises or duties levied for specific purposes were to be shared between the Union and the State governments at the ratio of 80 p.c. and 20 p.c. As regards the share of each State, it recommended that 80 p.c. of the net proceeds of the divisible pool should be distributed on the basis of population, and 20 p.c. on grounds of social and economic backwardness as indicated by the *per capita* gross value of agricultural production, *per capita* value added by manufacture, percentage of workers to total population etc. As regards the sharing of additional excise duties in lieu of sales taxes on textiles, sugar and tobacco, the commissioner recommended that out of the net proceeds of the additional excise duties levied on these 3 commodities, 1 p.c. be assigned to the Union Territories, 1½% p.c. to Jammu & Kashmir, and 0·5 p.c. to Nagaland. Of the balance, the guaranteed amount of Rs. 3254 lakhs was to be set

apart, and the rest was to be distributed on the basis of the proportion which sales tax revenue collections in each State bore to the total sales tax revenue on all States over the years 1961-62 to 1963-64.

The Commission did not recommend any change with regard to the distribution of the net proceeds of the estate duty except raising the share of the Union Territories from 1 to 2 p.c. Nor did it suggest any change with regard to the distribution of the grant in lieu of taxes on railway fares. On the question of grants-in-aid, the Commission felt that it should confine itself, more or less, to the non-plan expenditure of the States, as the determination of the total amount of plan expenditure in each State, and the sharing of such expenditure between the Union government and the States was to be done by the Planning Commission. After assessing the revenue receipts and non-plan expenditure of different States for 1966-67 to 1970-71, and the amounts accruing to them as their share of the various taxes and duties, ten States were found to have revenue deficits aggregating Rs. 609·45 crores during the next 5 years. So the Commission recommended annual grants amounting to Rs. 121·89 crores, equal to one-fifth of the aggregate deficit. This amount is to be distributed among Andhra Pradesh, Assam, Jammu & Kashmir, Kerala, Madhya Pradesh, Madras, Mysore, Nagaland, Orissa and Rajasthan.

The net result of all these recommendations with the percentage shares of the States is given in the following table :

	Share of income tax	Union Excise Duties	Additional Excise Duties	Estate Duty	Grants in lieu of Rly Fares tax
States' Shares	75%	20%	97·45%	98%	
Distribution	%	%	%	%	%
A. P. ..	7·37	7·77	7·42	8·34	9·05
Assam ..	2·44	3·32	1·98	2·75	2·79
Bihar ..	9·04	10·03	6·17	10·76	9·99
Gujarat ..	5·29	4·80	7·43	4·78	7·11
J & K ..	0·73	2·26	+	0·83	—
Kerala ..	3·59	4·16	5·65	3·92	1·85
M. P. ..	6·47	7·40	4·62	7·50	9·85

	Share of income tax	Union Excise Duties	Additional Excise Duties	Estate Duty	Grants in lieu of Rly Fares tax
States' Shares	75%	20%	97·45%	98%	
Distribution	%	%	%	%	%
Madras ..	8·34	7·18	11·13	7·80	5·81
Maharashtra ..	14·28	8·23	19·87	9·16	8·98
Mysore ..	5·14	5·14	5·21	5·46	3·98
Nagaland ..	0·07	2·21	+	0·09	0·01
Orissa ..	3·40	4·82	2·58	4·07	2·12
Punjab ..	4·36	4·86	5·01	4·70	7·43
Rajasthan ..	3·97	5·06	3·17	4·67	6·40
U P. ..	14·60	14·98	7·83	17·08	18·23
W. Bengal ..	10·91	7·51	11·93	8·09	6·40

The Commission also made a number of general suggestions *viz.*, the setting up of a permanent organisation in the Ministry of Finance for making a continuous study of various matters required by the Finance Commissions, the Constitution of a competent body to discuss the entire problem of the indebtedness of the States etc. Two members have again raised the question of providing a clear definition of the respective functions of the Finance Commissions and the Planning Commission.

These recommendations with some modifications rendered necessary by the fact that the Commission had no time to discuss certain matters have been accepted by the government. This Commission has also merely followed the lead given by the 3 earlier Commissions. The whole idea of a revision of the manner of distribution of revenues between the Union and the States after every five years is fraught with difficulties and usually leads to a good deal of manipulation just on the eve of the working of the commissions. It may be better to have a more or less permanent autonomous commission dealing continuously with these matters.

Questions

1. Describe the division of central and provincial sources of revenue under the Government of India Act of 1935.

2. Describe the main features of the system of provincial finance existing before 1950.

3. Describe the distribution of the sources of revenue between the Centre and the States under the present Indian constitution. How far is it an improvement upon the previous system?

4. "Resources must follow functions." Do you agree? How far is a system of division of financial resources on the basis of population satisfactory in the structure of federal finance?

5. Give a brief outline of the recommendations of the Indian Finance Commissions.

6. Write notes on: (*a*) the Niemeyer Award, and (*b*) the Deshmukh Award.

CENTRAL FINANCES

Main sources of revenue : The Central or Union Government enjoy the revenue from the following sources, *e.g.*, Import and Export Duties, Union Excise Duties, Corporation tax, Personal Income tax, Railways, Posts and Telegraphs, Currency & Mint including profits of the Reserve Bank. Of these sources 20 p.c. of the proceeds of the union excise duties on 35 commodities are to be handed over to the States. Of the personal income tax collections, $66^2/_3$ p.c., after excluding the proceeds of the surcharge, are distributed among the States.

The main heads of expenditure are the following, *e.g.*, defence services, civil administration including all the civil departments of the Union Government, debt services, civil works, contributions and miscellaneous adjustments between the Union and State Governments including the grants-in-aid, extra-ordinary items including the grants to the States on account of the GMF schemes community development scheme, industrial housing schemes, relief in natural calamities etc.

The over-all budgetary position will be evident from the following table :

TABLE I

Heads of revenue and expenditure of the Union Government

	Heads of revenue		1938-39	1957-58	1966-67 (Budget)
1.	Customs ..	..	40·51	179·99	5·67
2.	Union Excise Duties	..	8·66	273·62	7·99
3.	Corporation Tax	..	2·04	56·13	3·76
4.	Taxes on Income	..	13·04	90·27	1·64
5.	Estate Duty ..	.	—	2·31	8·10
6.	Currency & Mint	..	0·56	26·04	47·12
	(Profits of the Reserve Bank)	..	(0·20)	—	—
7.	Railways	..	1·37	6·29	32·61
8.	Posts & Telegraphs	..	0·19	3·71	4·17
9.	Total revenue	..	84·47	673·38	2481·12

	Heads of expendiure	*1938-39	1957-58	1966-67 (Budget)
1.	Defence Service ..	46·18	256·72	797·67
2.	Civil Administration ..	10·90	126·25	110·08
3.	Debt Services ..	14·12	42·08	414·83
4.	Contributions and Miscellaneous adjustments between Union and State Governments	3·06	45·96	401·33
5.	Social and Development Services	0·01	10·00	231·43
6.	Total Expenditure ..	85·11	691·33	2169·90
7.	Surplus (+) or Deficit (–) ..	–0·64	+42·05	+3111·22

This table will give an idea of the relative importance of the different sources of revenue, and of the heads of expenditure. We propose next to discuss the different items separately.

Income tax : Income tax was first introduced in 1860, withdrawn in 1865, and was again imposed in 1869. It was again withdrawn and re-imposed five years later. Since then it has remained a most important feature of the Indian tax system. In recent years about 35 p.c. of the total tax revenue is derived from the income tax.

The income tax consists of four different types of levies. There is, first of all, the Corporation tax, levied on the profits of all joint-stock companies. Revenue from this source is enjoyed exclusively by the Union Government. Secondly, there is the personal income tax levied on wages, salaries, business and professional incomes above a certain level. Thirdly, there is a super tax, *i.e.*, income tax levied at specially high rates, in addition to the ordinary rates, on incomes above a certain large amount. At present incomes above Rs. 20,000 a year have to pay a super tax at rates varying from 8% to 47·5%. Revenue from these two types of levies is shared between the Union and the State Governments, the former retaining 45 p.c. of the total revenue on these accounts. Lastly, for the purpose of the Union an additional surcharge

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* Figures for 1938-39 relate to undivided India.

† These are original budget estimates and do not take account of later changes.

at 10 p.c. has been levied. A part of this additional surcharge liability can be discharged through the Annuity Deposit Scheme.

Characteristics of the income tax : Certain characteristic features of the system of income tax must also be noted. The tax is highly progressive, the minimum rates being 5 P in the rupee *plus* a surcharge of 2½ p.c., and the maximum ordinary rate is 25 P in the rupee, payable by those with incomes between Rs. 15,000 to Rs. 20,000 a year, *plus* a surcharge of 10 p.c. Those with incomes above Rs. 20,000 have to pay a super tax, varying from 18 P in the rupee to 53 P in the rupee, so that the highest rate (including the super tax and the ordinary rate) is 78 P in the rupee on incomes above Rs. 1·5 lakhs *plus* a surcharge of 20 p.c.

Secondly, in calculating the total assessable income of an individual, his agricultural income, if any, is not taken into account. Agricultural income was originally subjected to tax, but was exempted from the year 1886 without much justification. At present agricultural income tax has been levied by some States as the tax has been placed on the State List. This is an anomaly, and ought to have been given up in the new constitution.

Thirdly, in calculating the assessable income, an allowance is made for depreciation, repairs, interest on borrowed capital etc., from the gross income. Professional expenses are also deducted from the income. Life insurance premia paid by the assessees, upto one-sixth of his total income or Rs. 10,000, whichever is less, are exempt from taxation. Similarly, donations made to well-known charitable institutions are also exempt from taxation upto 10 p.c. of the total income or Rs. 2 lakhs, whichever is less.

Fourthly, the tax is levied on the "slab system," introduced from 1939. According to this system, the entire income of an assessee is divided into slabs, arranged one upon another. No tax is levied on the lowest slab, while the rate of tax is the highest on the topmost slab. Let us suppose that a man earns a total income of Rs. 20,000 a year. Under the present Act, he would not pay any tax on the first slab of Rs. 2,000. On the second slab of Rs. 2,000 he will have to pay tax at the rate of 3% in the rupee. On the third slab, *i.e.*, that between Rs. 5001 and Rs. 7,500, he will have to pay tax at the rate of 6 p.c. in the rupee ; on the fourth slab (*i.e.*, between Rs. 7,501 and Rs. 10,000)

he will pay tax at the rate of 9 p.c. in the rupee ; and on the fifth slab (*i.e.*, between Rs. 10,001 and Rs. 12,000) he will pay tax at the rate of 11 p.c. in the rupee and so on. Under the "step system", which prevailed before 1939, the tax had to be paid highest rate applicable to an income of Rs. 20,000 a year is 25 p.c. in the rupee, the assessee in the step system would have to pay the tax at the rate of 25 p.c. in the rupee on his entire income, *i.e.*, Rs. 20,000. Whereas under the slab system, the highest rate would be applied only to the topmost slab, *i.e.*, on Rs. 15,001 to Rs. 20,000. The slab system is considered more equitable, and the tax liability increases gradually as the income rises and steep jumps are avoided. The slab system is based on the principle that to all persons the earlier units of income are highly valuable and should, therefore, be taxed more lightly.

Fifthly. the income tax system recognises the distinction between earned and unearned income. If the whole of the income is earned, it is granted relief to the extent of one-fifth of the income, subject to a maximum of Rs. 4,000. This distinction has been made on the principle that a person who has to work to earn his income has a lower taxable capacity than another who earns his income from investments.

Another important feature introduced recently is the rebate granted to the married persons and also to persons with children. This is a welcome recognition of the fact that the taxable capacity of an individual who has to support a wife and children is less than that of another who has no wife or child. In the budget of 1957-58, it was laid down that in the case of a married assessee, no income tax would be levied on the first Rs. 2,000 of his income, and a maximum exemption of Rs. 600 (Rs. 300 per each child) would be granted to those with children. Under the present Law a married person with two or more children will not have to pay income tax on the first Rs. 3,600 of his income. These rebates will not, however, be granted to assessees having an annual income of Rs. 20,000 or more.

Sixthly, provisions have also been made to introduce the "pay-as-you-earn" principle in the tax system. Normally the income tax is assessed on the last year's income or profits. That is, the income earned

in 1954 will be taxed in 1955. But persons whose incomes exceed Rs. 6,500 a year may be asked by the Department to make advance payments of their income tax. In other words they would have to pay in 1954 income tax on the income earned in the same year, either on the basis of their last year's income or on the basis of their own estimate of the present year's income. Previously the government used to pay interest at the rate of 2 p.c., on this advance payment of tax. But this has since been replaced. If the assessee pays the advance payment on the basis of his own estimate of income for the current year, he may have to pay a penalty rate of interest if his estimated income falls short of his actual income, as determined afterwards, by more than 20 p.c.

Lastly, the income tax Act makes it obligatory in all persons to submit a return of his income, whether taxable or not, to the authorities. But there will be no penalty for a person not submitting his return if his income is less than the minimum exempted limit. At present the minimum is Rs. 3,000 for a single individual and Rs. 6,000 for an undivided Hindu joint family. But if his income exceeds the minimum, he will be liable to pay a penalty if he does not submit a return of his income.

In calculating the income of a person, the income of his wife, and minor children will also be added together along with his own income.

Though in 1947-48 the effective rates of income tax in India were actually higher than those existing in even some of the advanced countries, the present rates are lower than those prevailing in the U.K., or the U.S.A. The minimum exemption limit is also higher in India than that in the U.K. But against this one must remember that the Indian taxpayer gets no rebate on account of the number of dependents, whereas this is the case in the U.K.

The number of taxable persons has increased considerably in India. The number of persons assessed to income tax was 285,940 in 1938-39. Their number has increased to 445,506 in 1949-50 and to 8,40,000 in 1958-59. The super tax is paid by a comparatively small number of

persons. In 1938-39, only 4,210 persons, *i.e.*, 1·4 p.c. of the total paid super tax, having an income exceeding Rs. 25,000. In 1958-59 the number of super tax payers increased to 7·5 p.c. of the total. But these 7·5 p.c. of the assessees paid a 88 p.c. of the total income tax collection. Thus in India only one person out of every 560 pays income tax as compared to about 30 persons out of every 100 in the U.K., or the U.S.A. Due to the extreme poverty of the people of this country, only a small number of persons possess incomes above the exemption limit. In spite of this, taxes on income including the corporation tax amounted to 30 p.c. of the total revenue in India in 1960-61 as against 54 p.c., in the U.K., and 85 p.c. in the U.SA.

It has been urged by a large section of opinion that the rates of income tax prevailing in India are proving very onerous, and are actually hampering the process of formation of capital. India is an under-developed country and needs a large amount of capital for the development of her resources. But the present rates of tax are leaving no incentive to persons who want to invest their savings and so help in capital formation. But as Prof. J. P. Niyogi has pointed out in his article that in view of the large-scale evasions now practised by many of the assessees, the effective rates could not be stated to be very high. For example, a person with an actual income of Rs. 10.000 per month succeeds in concealing Rs. 4,000 from the tax authorities. So he pays income tax on Rs. 6,000 while the remaining Rs. 4.000 escape taxation. As a result, even if it is admitted that the actual rates of taxation are high, the effective rates are not so. In reply to Dr. Niyogi's point the supporters of the first contention have argued that it was the high rates of taxation that led to large-scale evasion. But one must also remember that it has long been a frequent complaint that the income tax is evaded by a large number of persons even in years when the tax rates were lower than those ruling at present. Moreover, the government needs a certain amount of revenue to meet its expenditure. If the extent of evasion were considerably less, the government would be in a position to raise the same sum of revenue at lower rates of taxation. In other words, it is the large-scale evasions which are responsible for the present high rates of taxation, and the more honest taxpayers have been obliged to pay taxes at higher rates because such a large number of income-earners are dishonest.

TABLE II

Revenue from income tax including corporation tax

(Crores of rupees)

Year		Corporation tax†	Income tax on other incomes*	Total	Percentage of total tax revenue
		(1)	(2)	(3)	(4)
1938-39	..	2·04	15·24	17·28	22·9
1939-40	..	2·38	16·99	19·37	22·5
1944-45	..	83·65	107·65	191·30	68·1
1945-46	..	84·06	94·45	178·51	57·2
1946-47	..	68·85	91·74	160·59	52·2
1948-49	..	62·26	119·50	181·76	50·2
1951-52	..	41·41	146·19	187·60	36·2
1952-53	..	43·80	141·43	185·23	41·7
1953-54	..	41·54	122·04	164·38	46·8
1954-55	..	37·33	122·26	159·59	38·1
1955-56	..	37·04	131·86	168·40	39·3
1956-57	..	51·18	151·76	202·94	41·1
1957-58	..	50·13	163·20	219·83	38·2
1958-59	..	54·33	172·01	226·34	40·9
1959-60	..	106·56	148·85	255·41	39·7
1960-61	..	111·05	167·38	278·43	37·4
1961-62	..	156·46	165·39	321·85	36·8
1964-65	..	314·05	266·55	580·60	37·1
1966-67 (Budget)	..	376·07	294·45	670·52	34·5

Corporation tax : The tax is levied on the income of registered firms and joint-stock corporations, at the maximum rate of 50 p.c. in

* Includes States' share of the income tax.

† Includes the revenue from E. P. T., Business Profits Tax and Capital Gains Tax when levied.

the rupee. The undistributed profits of these companies are also assessed to tax.

The tax was first levied in India after the World War I. At first there was an exemption limit below which no tax was levied, as in the case of the personal income tax. Thus during 1938-39 no corporation tax was levied if the profits were below Rs. 50,000. But this exemption limit was abolished by the Finance Act of 1939, and from that year all profits or income of joint-stock companies are assessed to this tax.

Customs : Under the present constitution customs is an exclusive source of revenue of the Union Government. Formerly the jute-growing States received a share in the proceeds of the Jute Export Duty, and it was also laid down that the Government of India might hand over a part or whole of the proceeds of any export duty to the States. These provisions have been deleted from the present constitution, though the jute-growing States would receive grants-in-aid in lieu of a share of the Jute Export Duty for the next 10 years.

Customs consist of two kinds of duties, import duties and export duties. *Duties on imported goods* have been levied in India from a very long time. Originally these import duties were levied for purposes of arising revenue. But since the adoption of the policy of discriminating protection from 1923, a number of such duties have been levied for the potection of domestic industries. The yield from such duties has, however, declined proportionately with the development of domestic industries. Besides these protective duties, there is a general rate of import duties applicable to all imports with certain exceptions. Foodgrains, pulses and a number of industrial raw materials are imported duty free. A specially low rate is charged on a large number of essential imports like fuel oils, lubricants, textile machinery, raw films etc. Luxury goods like wines and spirits, artificial silk goods, clocks and watches etc., are subjected to very high rates of duty, varying from 75 p.c. to 100 p.c.

Import duties may be of two types, *specific* and *ad valorem*. When the duty is levied on the basis of the weight or certain other characteristics of the commodity, it is known as a specific duty. When the duty is levied on the value of the imported commodity, it is known as the *ad valorem* duty. *Ad valorem* duties tend to be progressive as their incidence rises with higher prices. But they give rise to evasion as

importers try to declare lower values for imports. Specific duties are easy to administer and less liable to evasion. But their burden increases during depression. In the Indian customs schedule, *ad valorem* duties are levied on about 55 to 75 p.c. of the total imports.

Export duties. In recent years such duties have been levied on a large number of articles, and the yield from these duties increased from 4·8 p.c. of the total revenue from customs in 1946-47 to 23 p.c., in 1954-55. Before the last war these duties were levied mostly on raw and manufactured jute, rice and tea. Small cesses were also levied on tea, coffee and some agricultural products. But the proceeds of these cesses were utilised either for the expansion of the markets for tea and coffee, or for financing research. Subsequently export duties have been levied on raw cotton and cotton cloth, mustard oil, iron and steel products, etc. Following devaluation the government raised the rates of duty on most of these products in order to appropriate the profits arising from devaluation for the Treasury. The outbreak of the Korean war led to a further rise in the foreign prices of certain export commodities, and the government again enhanced export duties through an Ordinance. Gradually as prices began to fall in the international markets, these export duties were reduced, until some of them have been abolished altogether in order to improve the competitive position of these exports in the foreign markets.

The export duties are mostly specific. In view of the fact that the incidence of these duties is most likely to fall on the domestic producers, they are likely to discourage production and exports. Hence the Fiscal Commission of 1922-23 expressed the opinion

(1) that export duties should only be levied on articles of which India has a complete, or at any rate, a partial monopoly.

(2) that in any case the rates should be low.

(3) that an export duty should not be utilised for the purpose of protecting an industry.

The gradual importance of customs as a source of revenue will be evident from the table III, as compared to income tax.

TABLE III

Revenue from Customs (crores of rupees)

Year	Import Duties	Export Duties	Total Customs	Percentage of total tax revenue
1938-39 ..	38·91	1·60	40·51	54·8
1945-46 ..	781·	2·18	73·61	26·1
1950-51 ..	109·79	47·36	157·15	44·0
1951-52 ..	140·95	90·74	231·69	50·4
1952-53 ..	117·78	55·97	173·75	47·0
1955-56 ..	127·98	37·76	166·70	25·6
1957-58 ..	150·94	26·83	179·99	31·1
1959-60 ..	135·82	14·89	180·71	26·1
1960-61 ..	154·61	13·12	167·73	24·0
1964-65 ..	404·64	2·43	407·07	20·0
1966-67 (Budget) ..	507·40	2·07	569·47	24·9

In 1944-45, the revenue from income tax amounted to 68·1 p.c. of the total tax revenue, whereas that from customs amounted to only 15·7 p.c. Since that year, the revenue from the customs has increased in importance until as before the war it occupies the first place among all sources of revenue of the Central Government.

Union excise duties : Excise duties are taxes levied on goods produced and sold within the country. Under the present constitution (which follows in this respect the pattern of the Government of India Act of, 1935), excise duties on home-manufactured drugs, narcotics, hemp, alcoholic liquors etc., are levied by the State Governments. Excise duties on other domestic products are levied by the Union Government, and hence are known as the Union excise duties.

Union excise duties have been levied on sugar, matches, kerosene, motor spirit, steel ingots, tobacco, vegetable ghee, tyres, tea, coffee, cotton cloth etc.

Excise duties tend to raise prices and so restrict both production and consumption. In order that they may yield sufficiently large revenue, they have to be levied on goods of comparatively inelastic demand. But since such commodities are generally necessaries, they tend to fall more heavily on the poor. For these reasons the Fiscal Commission of

1922-23 laid down the following conditions for the levy of excise duties:—

(1) In order to minimise the cost of collection, excise duties should ordinarily be confined to industries which are concentrated in large factories or small areas.

(2) They might properly be imposed to check the consumption of injurious articles like drugs, alcoholic liquors etc.

(3) They might be levied on commodities of general consumption, but should not press too heavily on the poorer classes.

(4) When a protected commodity is taxed there should be an equivalent additional import duty.

Excise duties are playing an increasing role in central finance. Their yield has increased from Rs. 8·65 crores in 1938-39 to Rs. 700·00 crores in 1963-64, and their percentage contribution to the total tax revenue has increased from 11·7 p.c. in 1938-39 to 56·1 p.c. in 1963-64. Most of these duties have been imposed during the war to make up for the loss of revenue from the customs. They have been found to be a good means for the purpose of taxing small incomes which have increased during the war and post-war years due to the prevalence of inflationary conditions. As a result of the imposition of such duties on a large number of commodities, they have become more broadbased than formerly. Some of these duties have proved to be very productive, for example, the duties on tobacco, cotton cloth, sugar and matches constitute nearly 80 p.c. of the revenue from all Union excise duties. Tobacco has everywhere been recognised as a suitable object of taxation. It is widely consumed and is recognised as a luxury. A tax on tobacco was recommended by the Taxation Enquiry Committee of 1925-26, but its imposition was postponed on account of the administrative difficulties of collection. Tobacco is generally grown in small areas and did not pass through any well-organised trade channel on which duties might be levied. But the exigencies of the war finance and the growth of a cigarette manufacturing industry in India under the shelter of revenue duties have made it possible for the government to levy this duty. In 1963-64 it alone was expected to yield a revenue of Rs. 100 crores out of a total of Rs. 700 crores from all Union excise duties.

The great defect of these duties is, as has been pointed out, their regressive character. Many of the excise duties like those on matches,

kerosene, sugar, tea and cloth are levied on commodities consumed mostly by the poor and the middle classes.

As has been stated previously, under the award of the Four Finance Commissions, 20 p.c. of the proceeds of the excise duties on all articles is distributed among the States on the basis of their populations.

TABLE IV

Revenue from excise duties

Year	Revenue from excise duties	Percentage to total tax revenue
1938-39	8·65	11·7
1939-40	6·53	8·1
1945-46	46·36	16·5
1948-49	50·65	15·8
1950-51	67·54	19·0
1952-53	83·03	18·7
1955-56	145·25	33·9
1957-58	273·62	47·6
1959-60	360·65	57·3
1960-61	394·98	56·2
1961-62	489·31	57·0
1964-65	801·51	59·0
1966-67 (Budget) ..	1022·04	56·1

The Estate Duty Act : The question of the levy of death duties has been discussed in India from a long time. The term, death duties, is generally applied to taxes levied on the transfer of property after the death of an individual to his heirs. In one form or other, these duties form an important feature of the tax systems of almost all advanced countries. They may be levied on the total property passing after death, when they are known as estate or succession duties. Or, they may be levied, in the form of inheritance tax, on the share of the property of the deceased received by each heir. Lastly, the rates of death duty may be graduated on the basis of the relationship of the heirs to the deceased, the nearest in relationship paying duty at the lowest rates. Very few economists dispute the justice of the imposition

of death duties. They are levied on the basis of ability and are usually collected at a time most suitable to the taxpayers who can easily pay them out of the proceeds of the inherited property. These duties supplement the income tax. An income tax, however carefully devised, cannot take into account all the relevant considerations bearing on the principle of ability. For example, income tax does not usually cover unearned increments in the value of property, stocks or bullion or jewellery. But these can be taxed through death duties. A tax system which combines both income tax and death duties for raising a given amount of revenue is much better than another which relies only on the former to collect the same amount of revenue.

The question of imposing death duties in India was considered in detail by the Taxation Enquiry Committee (1924-25). That Committee pointed attention to certain difficulties standing in the way of the introduction of the death duty. In particular, it mentioned the case of the *mitakshara* joint families where there was virtually no inheritance, the sons automatically received a share in the ancestral property from the moment of their birth. The Government of India Act of 1935 included a provision whereby the Central Government was given the right to levy duties on succession to property other than agricultural land. But the proceeds were to be distributed among the Provinces. Duties on succession to agricultural land remained a State subject. Similar provisions have also been included in the new constitution. In 1948, the government introduced the first Estate Duty Bill in the legislature. A Second Bill was introduced in March, 1948. Both these Bills were allowed to lapse. A third Bill had better luck, and was finally passed into an Act in 1952, and came into force from October, 1953. It should be noted that prior to 1935, small duties were levied on property passing at death in the form of Probate and Succession Duties. These duties, levied at the rate of 5 p.c., were to be paid by all persons who left a will to dispose of their property for which it was necessary to take out letters of administration or succession certificates. Hindus and Muslims who died intestate thus escape these duties. As such these were highly inequitable.

Under the Estate Duty Act of 1953, the tax is to be assessed on the entire estate of the deceased, including cash, bullion, jewellery, household effects, motor cars, shares and securities, loans due from debtors etc. All *bonafide* debts of the deceased are to be deducted from

the value of the assets. All gifts, unless made two years before death, are to be included. But gifts for public charitable purposes made before six months of death are to be excluded. But small gifts up to the maximum of Rs. 2,500 made for public charitable purposes and of Rs. 1,500 made for other purposes are to be excluded even made within six months or two years of death as the case may be. Similarly, a life insurance policy up to Rs. 5,000 or an insurance policy made for the payment of the estate duty up to the maximum of Rs. 50,000, is exempt from the duty.

No duty is payable if the value of the property does not exceed Rs. 1,00,000 in the case of individuals, and Rs. 50,000 in the case of an interest in the *mitakshara* joint family property. In the case of individuals, the lowest rate of duty is 7½ p.c. to be levied on Rs. 50,000 in excess of one lakh. That is, properties left by a person worth Rs. 15,000 will have to pay duty of Rs. 3,750 or at an average rate of 2·5 p.c. The maximum rate of duty is 40 p.c. to be levied on properties in excess of Rs. 20,00,000. That is, if a person leaves properties worth one crore of rupees, his successors will have to pay a little more than thirty-four lakhs of rupees in estate duties.

The heirs will have to submit within 6 months of the death of the individual a return showing the list and value of the property left at death. The duty would have to be paid within two months from the date of assessment. The sum assessed may, however, be paid in instalments in certain cases. In order that a property may not be assessed to this duty in quick succession if a second death follows very soon after the first, it has been provided that no duty would be levied on a property if the widow dies within seven years of the death of her husband. In the case of other heirs, if a second death takes place within 5 years of the first death, an allowance to the extent varying from 50 to 10 p.c. would be made in the second assessment.

Comments on the Duty : The high exemption limit of rupees one lakh means that only a small percentage of the population of this country would have to pay this duty. This is a desirable feature. It takes time to get a skilled and efficient administrative machinery for the management of this duty. The difficulties of the valuation of property are also serious in this country where the stock exchanges are not well-organised and very few persons keep a complete record of accounts. Hence in the initial stages the member of assessees should be kept as small as is possible.

The question of the proper valuation of properties will of course present some difficulty in the initial stages. The capital value of landed property is rather difficult to assess as no tax on the capital value of land is levied anywhere in India. Similarly, there will be difficulties with regard to the valuation of personal business assets. These are, however, expected to be overcome in course of years as the administration gets more experience.

The most serious criticism that has been brought against this duty is that it will tend to discourage capital formation and will reduce the incentive to work and save. The question cannot be studied in isolation. The State Governments must raise additional revenues to finance schemes of development. The imposition of commodity taxes and other indirect taxes has already been carried to the limit. If the burden of development is to be distributed more equitably, recourse must inevitably be had to some form of direct taxation. The rates of income tax are already at very high levels, and it would scarcely be possible to raise additional revenue through the income tax without impairing the incentive to work and save to a greater extent than would be the case under the estate duty. Moreover, an estate duty is likely to retard capital formation to a smaller extent because it is, after all, a deferred tax, and a deferred tax is always felt less than a tax which has to be paid immediately.

There can, therefore, be no objection to the levy of an estate duty, especially in view of the great need to raise additional revenue for developmental purposes. The exemption limit is quite fair ; and the rates of duty are not onerous. One criticism of the details that can be made is that gifts for public charitable purposes should be exempted from the duty even if made at the time of the death. There is a great need to encourage the flow of funds for well-known public charitable purposes. When a person makes a gift of one lakh of rupees to (say) the university, it is not fair that the government should have a cut in the amount at the cost of the university funds. When such gifts are also exempt for purposes of income tax, there is no justification for not exempting them from the estate duty.

The wealth tax : In the budget proposals for the year. 1957-58, the Minister of Finance has introduced this new tax on the wealth of an individual, a Hindu undivided family or a company. The levy of this tax was considered by the Taxation Enquiry Commission, which, though favourably inclined, decided to drop the proposal on account

of administrative difficulties. The proposal to levy a tax on wealth formed an integral part of the scheme of tax reforms suggested by Mr. Kaldor in his Report on Income Tax Reform.

This tax is to be levied on the net wealth of an individual, and Hindu undivided family. All property, movable or immovable, is to be included in the calculation of net wealth with the exception of agricultural lands. The debts owed by the individuals are also to be excluded. But any property transferred to his wife and minor children is to be included in determining the net wealth.

The tax will be levied on all such persons who possess net wealth in excess of two lakhs of rupees. In the case of Hindu undivided families, the exemption limit is Rs. 3 lakhs and it is Rs. 5 lakhs in the case of companies. The tax will not, however, be levied on certain items of property such as furniture, wearing apparel, etc., intended for personal or family use, subject to a maximum of Rs. 25,000 in value. Life insurance policies, Provident Fund balances, certain Government securities like Treasury Savings Deposit Certificates etc. will not also be charged to this tax. In the case of an individual, property worth the first two lakhs of rupees are exempt ; the next Rs. 10 lakhs will be taxed at the rate of $\frac{1}{2}$ p.c.; the next Rs. 10 lakhs are to be taxed at the rate of 1 p.c., and the remaining property (*i.e.*, in excess of Rs. 22 lakhs) is liable to tax at $1\frac{1}{2}$ p.c. Thus an individual possessing net wealth of Rs. 5 lakhs will have to pay wealth tax amounting to Rs. 1,500. He will have to pay Rs. 4000 if his total wealth is valued at Rs. 10 lakhs. This tax is to be paid annually. The wealth tax on companies was abolished from April 1, 1960.

The wealth tax is like the income tax, paid annually at progressive rates with the difference that it is levied on property, while the income tax is levied on income. The income tax does not always satisfy the canon of ability to pay taxes. An individual may have a large income with quite small property, while another may have large property, but comparatively small income. The second man's ability to pay taxes is not less when account is taken of his income and property. A combination of the wealth tax and the income tax thus provides a bette' method for adjusting the burden of taxes to the total ability of individuals. This tax would thus contribute to the more effective taxation of the richer classes. Moreover, as Mr. Kaldor has pointed out, the levy of tax would result in checking tax evasion. If taxes are levied both on

income and on property by the same authority, the loopholes for tax evasion would be reduced to some extent. Thirdly, the government would have to raise large sums of money for financing the Five Year Plans, and for this purpose must raise additional revenue through taxes. The wealth tax is very appropriate as it touches only the large property owning classes, *i.e.*, those who have net property worth at least Rs. 2 lakhs. Lastly, this tax would discourage the holding of such property or investment that gives no yield or comparatively poor yield, such as bullion, jewellery etc. As such, more money will be available for productive investment instead of being hoarded in the form of gold or jewellery.

This tax has naturally given rise to a large outcry from the property-owning classes. It has been urged that this tax would impair incentives to the accumulation of wealth. Why accumulate property when you have to pay high taxes on it ? But it should be remembered that this tax will not be levied on people owning property worth less than Rs. 2 lakhs. Side by side with this tax, the rates of income tax have been lowered to some extent, thus providing some relief to the owners of large properties. A second objection is that the administrative difficulties involved in a satisfactory assessment of the tax would be formidable. Every item of property has to be valued, including wearing apparel, jewellery and a host of miscellaneous forms of wealth. Determination of the proper value of all forms of property is an extremely difficult task. The taxpayer would naturally declare as low a value as is possible, while the taxing officers will, in their turn, try to put as high a value as is practicable. There will be an enormous scope for bribery and corruption. Lastly, the levy of the tax on the wealth owned by the companies has also been criticised. A company is owned by the shareholders, many of whom would also be called upon to pay this tax on their wealth including the value of the shares owned by them in the company. As such, it means double taxation of the same property and so is inequitable. Mr. Kaldor did not suggest the inclusion of companies within the ambit of this tax.

There is no doubt that while this tax has some objectionable features, its levy is amply justified on three grounds, *viz.*, prevention of evasion of taxes, reduction of inequalities in the distribution of property, and raising sufficient revenues for financing the plan.

The expenditure tax : The Budget for 1957-58 also included the proposal to levy another new tax, *i.e.*, the expenditure tax. Unlike the wealth tax, which has been levied in some other countries, this tax

is being given the first trial in India. Mr. Kaldor, who is responsible for framing this tax scheme, submitted it before the Royal Commission on Taxation in Great Britain. But the Government in England did not accept his proposal. Mr. Kaldor included his scheme in his Report on Income Tax Reform, which he submitted to the Government of India.

The expenditure tax is to be levied on the expenditure incurred by an individual or a Hindu undivided family in the previous year. But no person whose annual income is less than Rs. 60,000 will have to pay this tax. In other words, only individuals who earn Rs. 5,000 or more per month will have to pay this tax on their expenditure. There are certain items of expenditure which will be deducted from chargeable expenditure. A basic allowance of Rs. 24,000 for the assessee and his wife and an allowance of Rs. 5,000 for each dependent child are to be exempt from taxation. In other words, if an individual has a wife and two children, he will not have to pay any tax on Rs. 34,000 of his total expenditure. Secondly, the business expenses of the assessee, expenditure on immovable property, investment in deposits, loans, shares and securities, repayment of loans, life insurance premium, and contributions to Provident Funds etc. are also to be exempted from this tax. Capital expenditure on the purchase of jewellery, ornaments, furniture, motor cars etc. is to be spread over five years, and only one-fifth of this expenditure is to be included in the chargeable expenditure in the first year.

The expenditure tax is to be levied at the following rates :—10 p.c. on the first Rs. 10,000 of the taxable expenditure, rising to 20 p.c. on the next Rs. 10,000 and so on until all expenditure in excess of Rs. 50,000 is to be taxed at 100 p.c. To take an example, let us take the case of an individual having a wife and two children, earning a total income of Rupees one lakh, out of which his expenditure is Rs. 64,000. A basic allowance of Rs. 24,000 and of Rs. 10,000 for two children will be exempt from taxation. So he would not have to pay the tax on Rs. 34,000. Expenditure from Rs. 34,000 to Rs. 44,000 will be charged at 10 p.c.; that from Rs. 44,000 to Rs. 54,000 at 20 p.c.; and that from Rs. 54,000 to Rs. 64,000 at 40 p.c. In other words, he will have to pay Rs. 7,000 in expenditure tax.

The principal advantage of a tax on expenditure is that it "is a most potent weapon for inducing economies in personal spending among the well-to-do classes." A progressive tax on expenditure is the

ideal instrument for cutting down luxury expenditure among the comparatively richer classes. Such people will naturally spend less in order to avoid the payment of the tax. As a result, savings would increase. A second advantage of this tax lies in the fact that it can be used as an instrument for preventing the evasion of taxes. A person who earns a large income will either spend it or save and invest it in different assets. By checking these three figures of income, expenditure and property, it will be possible to catch him somewhere if he is trying to evade the payment of the income tax. In the Kaldor proposals, the scheme of expenditure tax is combined with reduced rates of income tax. In other words, the income tax rates are reduced to some extent, as, in his opinion, the present high rates kill the incentive to work and earn. If these rates are reduced, it would increase the incentive to work. At the same time the tax on expenditure would increase the savings of the richer classes. Thus a combination of these two taxes would encourage more work and saving.

It has, however, been urged that this tax would give rise to a good deal of resentment among the taxpayers, especially if they are asked to submit details of their expenditure to the officers. To avoid this difficulty, Mr. Kaldor has stated that it would not be necessary to ask the taxpayer to submit details of his expenditure. If he submits statements of his income as he is doing now, and another statement of the additions to his property, the tax officer will find out his total expenditure by deducting the second from the first. Income will either be spent or saved and added to the assets. So by deducting the net addition to the assets from the income, one can know the amount of expenditure.

The tax on expenditure is a novel one, and has aroused a good deal of opposition. It would certainly have the effect of reducing consumption among the richer classes. The real question is whether the combined burden of income taxes (even though reduced), expenditure tax and the wealth tax would prove to be higher than that of the present. If this is so, some check to incentive and saving may result from these taxes. This tax has been repealed from the budget of 1962-63, revived again next year, and again repealed in the budget of 1966-67.

Capital gains tax : The term, capital gains, is applied to the profits received by the seller of a capital asset who succeeds in selling his particular asset at a price higher than that at which he acquired it. A person buys a share or government security to-day at Rs. 80/- per unit. He sells it after 3 months at Rs. 90. His capital gains amount to Rs. 10 per share. These gains are obtained from the appreciation of the value of the capital asset like a share or security or land or buildings etc. These gains are not counted as income for purposes of income tax. These gains are in the nature of a windfall, and by levying a tax on such gains the State attempts to absorb large slice of them for its own use.

A tax on capital gains was first introduced in India in 1947 by the then Finance Minister, Mr. Liaquat Ali Khan. It remained in force for 2 years when it was abolished. It was again re-introduced on the 30th November, 1956 by the Union Finance Minister, Mr. T. T. Krishnamachari. There are some important differences between the old system of capital gains tax and the new. Under the Liaquat Ali proposals, capital gains below the amount of Rs. 15,000 were exempted from this tax. In the new proposals, the exemption limit has been lowered to Rs. 5,000. But it has also been provided that no capital gains tax would be levied if the total of income and capital gains does not exceed Rs. 10,000. A second difference is that under the former system, capital gains were taxed on the basis of slab rates. It has, however, this defect that this bears no relation to the other income of the persons receiving the gains. But under the new Act, the rate of tax to be charged on capital gains should be the income tax rate applicable to the other taxable income of the assessee increasing by one-third of the capital gains he makes in the third year. Thirdly, the old Act did not levy any tax on the capital gains arising from the sale of residential property possessed by the assessee or his parent for 7 years or more. The new Act has dropped this exemption.

This tax has been subjected to strong criticism. Dr. John Mathai, who was the Finance Minister in 1949, abolished this tax as it did not yield large revenue as expected, and it exercised an adverse effect on investment and the free sale and purchase of stocks and shares. The question was considered by the Taxation Enquiry Commission which recognised that these gains were a fit subject for taxation. But it felt that the reasons given by Dr. Mathai in 1949 were still valid, and the

tax might stimulate tax evasion as the parties might attempt to pass off as capital gains what would otherwise have been treated as taxable income. The tax was, however, warmly commended by Mr. Kaldor, and formed an integral part of his scheme of tax reform.

There is no doubt that capital gains represent an addition to incomes and so increase the taxpayer's ability of pay. These gains also constitute one of the factors making for inequality of wealth. In a rapidly developing economy like ours, the extent of these gains would go on increasing at a fast rate, leading to large windfalls and a distortion of the pattern of income distribution. In his Report, Mr. Kaldor has sought to meet the criticisms of this tax. The argument that the yield from the tax was neither large nor a sound one. It would be a great mistake to treat the question of capital gains mainly on short-term revenue considerations. Moreover, he estimated that in view of the rising trend of production, prices and profits, the yield from this tax was likely to be quite large in the future. Secondly, this tax would prove to be an important factor in checking this evasion of taxes. It has, however, been argued that ths tax would bring about a distortion of the pattern of transactions in capital assets. In a period of capital gains, parties might be afraid of selling lest they would be called upon to pay high taxes. On the other hand, when the market is tending to go down, there might be a rush to sell in order to establish capital losses. As a result, the downward trend in share prices would be accentuated. The Indian investor, it is argued, buys a share not merely for annual returns but also in the hope that its value would appreciate in the long run. The levy of this tax, by absorbing a large slice of the appreciation of its value, would prove to be a definite disincentive to the small investors.

Compulsory savings scheme : In order to finance the expenditure on defence and development the Government of India has made savings compulsory from 1st July, 1963. "Like taxation compulsory savings will restrain demand in the immediate future, whereas unlike taxation, it would provide an earning asset to the people and generally help in improving the saving habit of the country." The Finance Minister expects about Rs. 40 crores annually from the scheme. A portion of the total collections will also be handed over to the States.

The scheme applies to people paying income-tax and salaried employees with annual incomes of Rs. 1500 or above but below the income-tax level. For Income-tax payers the maximum limits of the deposits are an amount equal to 3 p.c. of the residual income, where such income is Rs. 6,000 or less. Where it exceeds Rs. 6,000 the rate of deposits will be 3% of the first 6,000 and 2% of the balance.

For employees in the salary range of Rs. 1500 per annum and the floor limit of normal income-tax liability, the scheme provided for the compulsory deposit (to be collected at source) at 3% of the annual salary. In the Compulsory Deposits Act passed in May 1963, an exemption has been allowed to those employees of this category (non-income tax-payers), who are already contributing 11% of their income from salaries in the form of life insurance premia, contributions to provident fund, fixed postal deposits.

Under the scheme, depositors will be issued a separate pass-book in each case. The amount deposited together with simple interest at 4 p.c. per annum will be repaid five years after the end of the year in which the deposits are made.

The scheme has met with serious opposition, especially from people whose incomes range between Rs. 1500 and Rs. 3000 per year. It has been urged that families with monthly incomes of Rs. 125 or more are not in a position to save anything, as most of them are finding it extremely difficult to meet even the most necessary expenses. The result of the compulsory deposits scheme will be to force them to borrow. So it is doubtful whether the scheme will actually result in increased savings. The continuing rise in the prices of essential articles is further creating difficulties for these low income-groups. There would have been some justification for the scheme, had inflation been kept in control. But as prices continue rising week after week, the difficulties of these low income-groups continue to mount up. The scheme now applies to Income-tax payers only and non-income tax payers have been exempted.

Defence expenditure : India's defence expenditure has always been large. For example, it amounted to Rs. 47·22 crores in 1937-38, and formed 54·5 p.c. of the total revenue expenditure of the Government of India. It increased gradually during the last war, and stood at Rs. 395·47 crores, the highest amount ever reached, forming nearly 80 p.c. of the total revenue expenditure. It began to decline with the

end of the war, and further changes in the defence expenditure would be evident from table V.

TABLE V

India's Defence expenditure (crores of rupees)

Year		Defence expenditure	Percentage to total expenditure
1948-49	..	Rs. 146·05	45·5
1950-51	..	Rs. 164·13	46·7
1951-52	..	Rs. 170·96	44·1
1955-56	..	Rs. 172·23	38·1
1957-58	..	Rs. 256·72	40·7
1960-61	..	Rs. 230·88	31·4
1961-62	..	Rs. 247·55	30·0
1962-63	..	Rs. 451·81	27·8
1966-67 (Budget)	..	Rs. 797·67	36·7

The defence expenditure has thus increased after the achievement of independence, from Rs. 146·05 crores in 1948-49 to Rs. 205·62 crores in 1954-55 and to Rs. 256·72 crores in 1957-58. There is also no doubt that it consumes a very large part (more than 36 p.c.) of our budget. But one must frankly recognise that the scope for an effective reduction in the defence expenditure cannot be assumed to be large. If we study the defence expenditure in details, we shall find that 69 p.c. of the total defence expenditure is incurred on the army, 17 p.c. on the air force and only 5·8 p.c. on the navy. As against these percentages, the U.S.A. devotes about 39·1 p.c. of its defence expenditure to the air force, 34·4 p.c. to the army and 26·5 p.c. to the navy. So even if we succeed in reducing our expenditure on the army, which is extremely doubtful in view of Chinese aggression, we shall have to spend more money in the future on the expansion of the navy and the air force. An air force of reasonable strength is essential for the defence of the country, and India with its large coast line must have a large navy for the protection of the sea frontier. The only practicable scope for the reduction of the defence expenditures lies through overhauling the administrative machinery and eliminating waste and inefficiency. It is, of course, desirable that we should not spend so much on defence, but devote more

money to weilfare expenditure. But, to quote a classic statement, defence is greater than opulence, and India cannot, in view of the present world tension, afford to take risks with her defence.

Civil administration : The expenditure on civil administration of the Government of India has gone on increasing continuously from Rs. 35·36 crores in 1948-49 to Rs. 86·08 crores in 1954-55. It includes the expenditure incurred on the administration of the various civil departments of the Government of India, such as the external affairs, education, medical and public health, agriculture and rural development, industries, aviation, broadcasting, justice and jails, ports nd pilotage, light houses, tribal areas etc. While the increase in this expenditure is naturally looked upon with considerable misgivings, one must note the fact that the expenditure on industries, education, agriculture and the scientific departments amounted to Rs. 40·52 crores in 1954-55, forming 47 p.c. of the total expenditure on civil administration. In 1950-51, expenditure on these items constituted 33 p.c. of the total expenditure on civil administration, and amounted to Rs. 16·46 crores. Increase in expenditure on social and development services is certainly to be welcomed. This does not, however, mean that there is no scope for practising economy in this item of expenditure. The expenditure on the External Affairs Department, especially that on foreign embassies and missions, has gone on increasing, and there may be scope for some economy in this Department. A more careful watch should be kept over the expansion of the Staff of a Department. Government departments in India as in other countries have a tendency to expand beyond their reasonable requirements.

Public debts : The term, public debts, is applied to the loans contracted by the government of a country from its public or outside. Public debts may take various forms. At one extreme there are undated loans for which no definite time limit has been fixed for repayment, the government promising to pay interest at fixed rates. At the other end there are very short-term loans, payable on demand like the Post Office Savings Bank deposits. In between these two there are loans of various maturities from treasury bills repayable at the end of 3 months to long-term loans maturing at the end of 10 or 15 or more years. If the debts are contracted within the country, they are internal debts. If they are taken from foriegn countries, they are called external debts.

The following table will show the total public debts of the Government of India and their composition at the end of March of every year.

TABLE VI

Debt Position of the Government of India

(Crores of rupees)

End of March	Undated	Over 10 years	Below 10 years	Treasury Bills	Small Savings	Others	Total	External debts
1939	128.46	113.80	195.60	46.30	141.46	84.34	709.64	469.10
1945	284.03	396.80	531.94	86.71	159.18	113.39	1,571.42	38.13
1946	284.04	663.80	544.34	83.33	221.52	139.92	1,936.95	37.69
1948	257.74	682.42	572.85	98.68	233.10	244.42	2,089.21	29.83
1951	257.85	519 53	661.28	364.72	326.25	342.81	2,472.24	49.81
1952	257.85	463.47	682.19	332.51	372.57	351.24	2,459.83	136,99
1953	257.85	387.60	758.13	315 44	412.61	361.82	2,493.45	138.53
1954	257.85	271.43	834.99	334.95	448.51	355.44	2,503.17	136.44
1957	257.85	245.83	1,129.93	835.70	629.38	406.55	4,233.88	286 60
1960	257.85	707.48	1,472.91	1,297.60	856.87	530.99	6,301.33	630.50
1961	257.85	690.45	1,623.03	1,106.30	974.61	825.77	5,478.01	864.22
1966	257.84	765.28	2,401.80	1,611.82	1,527.12	1,602.92	8,165.78	2,629.18

It has been estimated that at the end of 1963-64, total interest bearing obligations would amount to Rs. 9056 crores.

Some explanation is necessary to understand the table. Undated debts are loans for which no definite date or year has been fixed for repayment. The government has promised to pay the interest at regular intervals and repayment will be made at the option of the government after giving several months' notice to the debt-holders. Debts repayable at the end of over 10 years or repayable at less than 10 years are long-term debts. Treasury bills are issued by the government with a maturity of 3 months. From 1949 this column, Treasury bills, includes Treasury Deposit Receipts. Small savings include the Post Office cash certificates, defence saving certificates, the National Savings certificates, Post Office Savings Bank deposits and 3½ p.c. 10-year treasury saving deposit certificates. "Other obligations" include (1) unclaimed balances of old loans which have ceased to bear interest from the date of discharge, (2) balances of ceased special loans, (3) balances of State Provident Funds, Pension Funds and other accounts, such as General Family

Pension Fund, the Hindu Family Annuity Fund, the Postal Insurance and Life Annuity Fund etc., (4) the amount of 3-year interest-free Bonds and 5-year Interest-free prize bonds. "External debts" consisted only of sterling debts till the end of March, 1949. But they include dollar loans from 1950.

A glance at this table shows that the total debts of the Government of India increased continually from Rs. 1205·76 crores on March, 31, 1939 to Rs. 2308·48 crores on March, 31, 1946. During these war years, the sterling debts declined from Rs. 469·10 crores in 1939 to Rs. 37·69 crores in 1946, while the rupee debts rose from Rs. 709·64 crores to Rs. 1936·95 crores in 1946, *i.e.*, by Rs. 1227·31 crores. The decline in sterling debts was brought about by the repatriation of these debts, and their substitution by rupee debts. Since then debts have been continually increasing till they stood at Rs. 2639·61 crores in March, 1954, *i.e.*, an increase of Rs. 664·97 crores since 1946. The amount of sterling debts declined continuously on account of repatriation until they stood at the nominal figure of Rs. 27·36 crores at the end of March, 1949. From 1950 the volume of external debts has increased on account of our dollar loans, which amounted to Rs. 16·77 crores, Rs. 24·60 crores, Rs. 112·04 crores, Rs. 113·74 crores and Rs. 111·80 crores at the end of March, 1950, 1951, 1952, 1953 and 1954 respectively. According to the budget estimates of 1963-64 the total interest-bearing obligations of the government would amount to Rs. 9056 crores at the end of March, 1964. It comes to a *per capita* debt of Rs. 210·4.

Against the estimated total debts of Rs. 7690·82 crores at the end of March, 1963, the Government of India owns interest-yielding assets of the value of Rs. 6496 crores. Thus the estimated uncovered debt at the end of 1962-63 has been estimated to amount to Rs. 1092·93 crores out of which Rs. 101·93 crores are held in cash and securities on Treasury account. Hence it is stated that India's debt position is sound as the amount of unproductive debts forms only a small part of the total. While this is a good position, a number of writers have criticised it on the ground that this orthodox position has been achieved by starving social and developmental services. The government, in their opinion, should have borrowed on a larger scale and utilised the money in improving the economic and social conditions of the people.

The interest charges on Central Government account amount to Rs. 414·83 crores according to the budget estimates of 1966-67.

Before 1924 there was no definite scheme for the redemption of debts. If there was any budget surplus in any year that was used to repay debts. In 1924 Sir Basil Blackett, the then Finance Minister, adopted a definite scheme under which debts were to be redeemed in course of a period of 80 years. During the years 1925-26 to 1929-30, the Government of India set apart every year the sum of Rs. 298 lakhs and paid it into a sinking fund for the redemption on debts. Since 1934-35 a lumpsum annual provision of Rs. 3 crores was made in the revenue budget for the reduction of debts. As the amount of debts increased during the war, the annual provision for the redemption of debts has been increased to Rs. 5 crores from the year 1946-47. Since then a sum of Rs. 5 crores is annually set apart from the revenue budget for repayment of debts.

Questions

1. Analyse the main sources of revenue and heads of expenditure of the Central Government.

2. Discuss the scope and importance of the Indian income tax.

3. What new changes have been introduced in the Indian income tax in recent years ?

4. Give a brief description of the various excise duties levied in India. Discuss the incidence of such duties. Examine the role of excise duties in India. (C. U. B. Com. 1957).

5. Describe the purposes for which import duties are levied in India. Examine the extent to which these objects have been realised.

6. Describe the desirability or otherwise of levying Death Duties in India.

7. Carefully examine the principal heads of expenditure of the Government of India. Review the policy underlying public expenditure in India.

8. State the case for and against the introduction of the capital Gains or the Expenditure Tax in India. (C. U. B. Com. 1961.)

9. Discuss the main features of (a) the Expenditure tax and (b) the Wealth tax levied in India. (C. U. B. Com. 1961.)

10. Give a short description of India's tax structure. Do you think that it is still possible to increase subsequently the tax revenue of the Government and how ? (C. U. B. Com. 1960.)

11. Discuss the attempts that have been recently made to reform the Indian tax structure. How far do you think the changes introduced would stimulate saving and investment. (C. U. 1960.)

12. Write note on the nature and classification of public debts in India. Do you think that our debt position is economically sound ?

Main sources of revenue of the States : Under the new constitution as modified by the award of the Finance Commission, the States enjoy the following sources of revenue ;—land revenue, stamps, registration, irrigation, forests, state excise duties, sales tax, agricultural income tax, tax on entertainments, betting, tax on electricity, etc. They also receive shares in the following central sources of revenue, *viz.*, 61·66 p.c. of the income tax (excluding corporation tax and central sur-charge), 20 p.c. of the revenue from certain Union excise duties on tobacco, matches and vegetable ghee etc. The proceeds of the estate duty which has been levied from 1953 is distributed among the States. Lastly, the States received grants-in-aid from the Central Government in different forms. Thus the jute-growing States received fixed grants-in-aid in lieu of the share of Jute Export Duties for a period of 10 years.

The importance of these sources of revenue has charged considerably since 1938-39. In 1938-39, the three main sources of revenue for the States were land revenue, stamps and excise duties. Sales taxes were not levied, and the share in the central taxes on income was comparatively small. In 1960-61 the main sources are the share of the income tax and union excise duties, sales taxes, excise duties on drugs, narcotics etc., land revenue and stamps. The importance of each of these sources in different States will be found from the tables given below.

TABLE I

Total revenue and expenditure in the States, 1966-67 (Crores of rupees)

	States Total Revenue	Total Tax Revenue	Income Tax	Land Revenue	Sales Tax	Excise Duties	Stamps
All States	2112	1279	132·91	120·48	407·86	305·36	74·18

	Total Expenditure	Development	Education	Medical Public Health	Agriculture Co-operation	Irrigation	Civil administration
Expenditure of all States	2086	1197	417	174	178	67	269

Excluding income tax, which is collected and distributed by the Central Government, the States raise their tax revenue mainly through land revenue, sales taxes and excise duties. Taking all States as a whole, land revenue still remains the sheet anchor in their finances, followed by the excise duties. But sales taxes are coming into prominence as an important source.

Main heads of expenditure : The main heads of expenditure relate to (*a*) general administration, (*b*) Justice and jails, and convict settlements, (*c*) Education, (*d*) medical and public health, (*e*) agriculture and rural development, (*f*) co-operation, (*g*) veterinary services, (*h*) industries, (*i*) irrigation, (*j*) civil works, (*k*) labour welfare, (*l*) debts services, (*m*) community development projects, (*n*) relief and rehabilitation, and (*o*) civil supplies etc. The Reserve Bank has classified these heads broadly into four groups, *viz*., debt services, civil works, security services and social services. Of the total expenditure incurred by all States amounting to Rs. 630·92 crores in 1957-58, Rs. 36·28 crores were spent on debt services, Rs. 56·15 crores on civil works, Rs. 91·19 crores on security services and Rs. 162·08 crores on social services. That is, 40·4 p.c. of the total expenditure was devoted to social services, and 22·6 p.c. on security services.

The expenditure on general administration formed 9·4 p.c. of the total expenditure of Part A States in 1954-55, and in Part B States it formed 5·6 p.c. One good feature was that the expenditure on education in all States increased from Rs. 11·65 crores in 1938-39 to Rs. 417 crores in 1966-67, forming more than 20 p.c. of the total expenditure. Expenditure on education was the highest in Bombay, being Rs. 26·58 crores, followed by U.P. (Rs. 17·27 crores), Madras (Rs. 15·50 crores) and West Bengal (Rs. 13·16 crores). *Per capita* expenditure on education was the highest in Bombay, being a little less than Rs. 4 per head, followed by 2·6 in West Bengal and Rs. 2·0 in Punjab. The *per capita* figure of Bombay was exceeded by that of Mysore, where it was Rs. 4·1. In Kerala, it was Rs. 3·6 per head. Expenditure on medical and public health had also increased in all States from Rs. 15·37 crores in 1948-49 to Rs. 15·31 crores in 1966·67 forming 8·0 p.c. of the total expenditure of the second year. *Per capita* expenditure in this department was the highest in West Bengal, being Rs. 21 per head, followed by Bombay (Rs. 1·39 per head). As against these increases in expenditure, that on police in all the States increased

from Rs. 35·52 crores in 1948-49 to Rs. 41·63 crores in 1954-55, forming 10·4 p.c. of the total expenditure. This increase was much less than that in respect of education or medical and public health. *Per capita* expenditure on police was the highest in Bombay (Rs. 2·57), followed by West Bengal (Rs. 2·44). It was the lowest in Bihar, being Rs. 0·95 in 1953-54.

Land revenue : Land is one of the earliest sources of income, and a tax on land has been levied in almost every country from very ancient times. Land revenue is the sheet anchor of state finance. The basis as well as the rates for the collection of land revenue vary in different States. Generally an attempt is made to assess the tax on the basis of the net income from land and the rate of assessment varies. Certain features are common to all systems of land revenue. First, land revenue is assessed at a flat rate, and the rate of tax does not vary progressively with the total income or the total holdings of the taxpayer. A large holder of land pays at the same rate as the cultivator tilling the smallest plot of land. The assessment varies with the grade of land, and takes no account of the type of crops grown. Thus the burden of land revenue is comparatively heavy on land growing cereals than that on land growing one of the commercial crops. Secondly, the assessment remains fixed for a certain number of years, irrespective of changes in prices or changes in yield. Thirdly, there is no minimum income which is exempted from assessment, whereas in the case of income tax, a minimum income is exempt from the tax. Hence the conclusion is inevitable that the system of taxation of land in India is not based upon any satisfactory principle.

In 1938-39 the yield from land revenue amounted to Rs. 25·40 crores in Part A States, forming 43·0 p.c. of their total tax revenue. In U.P., the yield formed 60 p.c., in Madhya Pradesh 55·8 p.c. and in Assam 55·5 p.c. of their total tax revenue. The lowest percentage contribution was in Bengal, being 29·5 p.c. With the rise in importance of other sources of revenue, land revenue has no doubt lost its position. But the yield from this tax has tended to increase in the last few years on account of the acquisition of zemindari estates by the States. Thus land revenue collections have increased in U.P. from Rs. 6·62 crores in 1949-50 to Rs. 21·28 crores in 1960-61, and to 27·57 in 1963-64, where it forms 40 p.c. of the total tax revenue. In Bihar, the yield has increased from Rs. 1·42 crores to Rs. 9·75 crores during the same

period, forming 28 p.c. of the total tax revenue of that State. In Madhya Pradesh, the yield from land revenue now forms 33 p.c. of the total tax revenue. In fact, the percentage of land revenue to the total tax revenue has risen in every State between the years 1952-53 to 1957-58. Among former Part B States, more than 74 p.c. of the total tax revenue was derived from land revenue in Saurashtra, followed by Madhya Bharat (37·5 p.c.), Rajasthan (31·4 p.c.), Pepsu (28·5 p.c.), Hyderabad (23·1 p.c.), Mysore (22·4 p.c.) and Travancore-Cochin, where it was only 9 p.c.

State excise duties : Under the present constitution, the States have been given the right to levy and collect excise duties on alcoholic liquors, opium, hemp and other narcotic drugs. Excise revenue also includes the licence fee for the sale of important liquor and licences for bottling it or other similar operations, though the import duty on such liquor is collected by the Union Government. States do not, however, have any right to tax medicinal and toilet preparations containing alcohol or drugs. The right to legislate for the levy of duties on these products belong to the Union Government, though the duties are administered and retained by the State Governments.

Excise duties also include the duty on country spirits and fermented liquors, whose manufacture is carried on either in private or government distilleries. In most States the right to sell the spirits at fixed prices is put upto auction. They also include the income from the sale and duty on opium, which is purchased from the Government of India.

The aim of the government is to raise the maximum revenue from this source while trying to maintain consumption at as low a level as is possible. These drugs and liquors are, therefore, subjected to high tax, the rates varying in different States. In 1938-39, the revenue from excise duties formed 22·2 p.c. of the total tax revenue of Part A States. In 1956-57, the revenue from this source amounted to 8·2 p.c. of the total tax revenue in Part A States and to 23·6 p.c. in the case of Part B States. This importance as a resource of revenue varies in different States. Among all States, the highest percentage is in Punjab, being 19·14 p.c. of the total tax revenue, followed by Bihar (15·9 p.c.), Orissa (15 p.c.), West Bengal (13·5 p.c.). The lowest is in Madras, where it is 6 p.c. of the total tax revenue. The small amount of revenue

from this source in Madras and Bombay (where it is 1·2 p.c.) was due to the adoption of a policy of prohibition by these States.

Sales taxes : Under the Government of India Act of 1935, the States obtained the power to levy a tax on the sale or purchase of goods. Hard-pressed to find additional revenue to meet the growing demands for funds for developmental purposes, the States have come to rely increasingly on the sales tax. The first State to levy sales tax was Madras which did it in 1939, followed by Bengal and Punjab in 1941, Bihar in 1944, Bombay in 1946. Among the Part A States U.P. was the last State to levy it in 1948. Part B States also levied this tax. The importance of this tax in State finances increased considerably over the last few years. In 1947-48 the total revenue for sales taxes on all commodities amounted to Rs. 18·87 crores in all States. By 1949-50, it has grown to Rs. 49·89 crores, and by 1960-61, it has increased to Rs. 117·96 crores, forming 21·3 p.c. of the total tax revenue of all States. In 1966-67, it would be Rs. 407·86 crores, forming 32 p.c. of the total tax revenue of all States.

Sales taxes are of two kinds—general sales taxes and particular sales taxes. General sales taxes are levied on all commodities, while particular sales taxes are levied on special commodities only like petrol, raw jute, tobacco etc. All States have levied sales taxes on motor spirits, while Bombay, Madras, Madhya Pradesh and Punjab have levied such a tax on the sale of tobacco. West Bengal has levied a sales tax on raw jute, and Bihar and U.P. on sugar cane. General sales taxes have been levied in all States.

A sales tax may be a single point or a multiple point tax. Under single point tax, the tax is levied on one point either on the first sale by producers or on the last sale to consumers. Bengal, Punjab, Bihar, Madhya Pradesh, Orissa and Assam have levied the single point tax.

Under the multiple point tax, the tax is levied every time there is a sale. Under this system a commodity may be taxed several times before it reaches the final consumer. Hence the rate of tax under the multiple point system is usually lower than that under the single point system. Madras followed this method. Bombay which originally introduced the single point system has changed over to the multiple point

system in 1952. Mysore and Kerala have also followed the Madras model.

The rates of sales tax vary in different States. In *West Bengal,* it is levied at the rate of 5 P. in the rupee at the retail stage only. Some important raw materials and a number of necessaries are exempt from the tax. Exports outside the State have not also been taxed. In *Madras,* dealers whose annual turnover exceeds Rs. 10,000 are taxed at 3 pies per rupee. In addition, a special tax of 6 pies in the rupee is levied on the sale of certain luxury articles such as motor vehicles, radio sets, cameras etc. In 1954-55 an additional single point sales tax of $1\frac{1}{4}$ as. per rupee has been levied on all mill-made cloth with the exception of certain coarse varieties. In Bombay, which adopted a single point tax and levied it at 6 pies in the rupee, has changed over to the multiple point tax. to make up for the loss of revenue due to the adoption of the system of prohibition. The general rate of tax of 3 pies per rupee and the minimum taxable turnover limit is Rs. 30,000. A number of articles of daily necessity and certain cottage industry products are exempt from taxation. *Punjab* originally levied the tax on the multiple point system. But in 1949 this has been changed to the single point system. The rate of tax has been fixed at 6 pies per rupee and the minimum taxable turnover limit has been fixed at Rs. 5,000 for importers, Rs. 10,000 for manufacturers and Rs. 30,000 for other dealers. In *Bihar*, the rate of tax is 6 pies per rupee, but that on certain luxury articles is 9 pies per rupee, while foodgrains are charged at 3 pies per rupee. The minimum taxable limit is Rs. 5,000. In *U.P.*, the government has levied a single point tax on some articles and a multiple point tax on others. The tax system is highly complicated. Even when the tax is single point the rate of tax varies from 3 pies to 6 pies per rupee, and it is levied on some commodities at the final stage and on some others at a different stage. The rate of tax under the multiple point system is 3 pies per rupee, levied on commodities not subjected to single point tax with the exception of certain essential commodities which are exempt from taxation. In *Madhya Pradesh* the general rate of tax is 6 pies per rupee levied on the single point system. Certain luxury articles are, however, taxed at the rate of 12 pies per rupee. In *Assam* and *Orissa* the general rate of tax is 6 pies per rupee, while some luxury articles are taxed at 1 anna per rupee.

This will show the multiplicity of tax rates and methods followed in different States. The need for securing some uniformity in regard to the levy of the sales tax in the States is, therefore, obvious. The lack of such uniformity has led to the competitive and multiple taxation of the same commodity in different States. This tax is highly regressive, though attempts have, of course, been made to provide some relief to the poorer classes by taxing essential articles of ordinary consumption at lower rates, or by exempting them altogether. Moreover, by levying taxes on luxury articles at higher rates, some progression has been introduced in the tax system. But luxury articles like motors cars generally pass through fewer hands, whereas commodities of everyday use like cotton textiles, foodgrains etc., pass through several dealers. Hence under the multiple point luxury articles are taxed on smaller occasions, while essential commodities may be taxed several times. The tax under the multiple point system thus tends to be more regressive than that under the single point system.

Agricultural income tax : Though the income tax is levied by the Union Government, the right to levy the tax on agricultural income has been granted to the States both under the Government of India Act of 1935 and the present constitution. This exemption of agricultural income from the levy of the general income tax began from 1886. There was of course no ground for such exemption, and the Taxation Enquiry Committee of 1924-25 also thought in the same way. But the exemption has been continued in both the Government of India Act of 1935 and the present constitution.

The first State to levy this tax was Bihar in 1938. Assam followed a year later, and at present this tax is levied in almost all States. The method of taxation, the minimum exemption limit and the rates of taxation vary in different States. Bihar levies the tax on the step system of taxation, the assessees being divided into 13 income groups. The minimum non-taxed income is Rs. 5,000, and the rates of tax vary from 6 pies in the rupee on those with incomes between Rs. 5,000 and Rs. 10,000, to 2 as. 6 pies per rupee on those with incomes above Rs. 15 lakhs. In Assam, West Bengal, U.P., and Rajasthan the slab system as in the general income-tax has been adopted. The minimum exemption limit is Rs. 3,000 in Assam, U.P., and West Bengal, and

Rs. 6,000 in Rajasthan. The rates of taxation vary from 9 pies to 1 anna per rupee on the first slab to a maximum of 2½ as. per rupee in Assam and West Bengal and 4 as. in U.P., Bihar and Rajasthan have also levied a super tax on the slab system on agricultural incomes exceeding Rs. 25,000 in the first two States and Rs. 30,000 in Rajasthan.

There is ample justification for the levy of this tax. In the past bigger landowners were also taxed at a flat rate. The land revenue system was not progressive, and so the land-owners did not bear a fair share of the tax burden. The introduction of this tax makes the land revenue system more progressive. In the past few years the revenue from this source has declined owing to the acquisition of all zemindari estates by the State.

The assessment of income tax by the Union Government and that of agricultural income tax by the State have given rise to a number of anomalies. When agricultural income is excluded from the calculation of total income for purposes of taxation, the rates of tax may, to that extent, be lowered. This results in some loss of revenue and inequity between taxpayers with no agricultural incomes and those with some agricultural incomes. The best course would be to authorise the Union Government to levy this tax by taking agricultural income into account in calculating the total income of the assessees. But the proceeds of the tax on agricultural incomes may be handed over to the States on the basis of collection.

Per capita revenue and expenditure in States : *Per capita* revenue and expenditure figures are sometimes used to compare the relative resources available to States and to examine the standards of public administration achieved by them. One must, however, remember the limitations in their use. They are not always a sure guide for purposes of comparison, as the yield from taxes depends on a large variety of factors and along with *per capita* expenditures, one must pay attention to the sparseness or otherwise of population and other factors to judge the standard of public administration reached by the States.

TABLE II

Per capita revenue of States

Name	Average of 1937-38 to 1946-47	1951-52	1952-53
Assam	4·3	11·0	12·5
Bihar	2·5	7·2	7·9
Bombay	10·7	16·8	16·8
Madhya Pradesh ..	4·3	9·1	10·8
Madras	5·7	10·2	10·5
Orissa	3·0	7·1	7·9
Punjab	6·9	13·4	14·1
U.P.	3·7	8·2	8·6
West Bengal	3·9	13·8	15·6
Hyderabad		13·8	15·6
Madhya Bharat ..		13·0	14·2
Mysore		15·8	15·6
Pepsu		16·1	17·0
Rajasthan		9·9	10·2
Saurashtra		19·0	18·3
Travancore-Cochin ..		15·0	19·2

A study of these figures showed that a wide difference existed in the *per capita* revenue of different States in the 10 years ending 1946-47. Thus Bombay had the highest *per capita* revenue at Rs. 10·7 while Bihar had the lowest at Rs. 2·5. Bombay's *per capita* revenue was thus more than four times that of Bihar. But in 1951-52 these differences had been narrowed down considerably. Among Part A States Bombay had still the highest *per capita* revenue. But its revenue was only two and a half times that of Bombay. The most significant change had occurred in the case of West Bengal whose *per capita* revenue in 1951-52 was four times that of undivided Bengal in the pre-paratition days.

Table III gives a picture of the *per capita* expenditure in States on selected services in 1951-52.

TABLE III

Per Capita Expenditure of States

Name	Administrative Services	Police	Social Services	Education	Medical & Public Health
Assam ..	2·5	1·1	3·7	1·9	0·9
Bihar ..	2·1	1·0	2·0	0·9	0·5
Bombay ..	4·6	2·6	5·7	3·4	1·2
Madhya Pradesh ..	2·4	1·2	2·4	1·4	0·4
Madras ..	3·1	1·3	3·6	1·9	0·9
Orissa ..	2·1	0·9	1·9	0·9	0·5
Punjab ..	4·0	2·1	3·0	1·5	0·7
U.P. ..	2·3	1·2	2·4	1·2	0·5
West Bengal ..	4·2	2·3	4·1	1·4	1·7
Hyderabad ..	3·8	2·8	3·6	2·2	0·8
Madhya Bharat ..	3·8	2·0	4·2	2·0	1·3
Mysore ..	2·2	1·0	5·7	3·1	1·3
PEPSU ..	4·3	2·2	3·3	1·7	0·9
Rajasthan ..	3·0	1·5	2·8	1·5	0·9
Saurashtra ..	6·8	2·9	5·1	2·8	1·5
Travancore-Cochin ..	1·8	0·7	4·4	2·7	1·2

While the differences in the *per capita* expenditure on police were not very large, the differences with regard to the expenditure on the social services were substantial. The average expenditure on the social services in Part B States was larger than that in the Part A States. The expenditure on education was higher in most of the Part B States than that in the Part A States with the exception of Bombay. The *per capita* medical expenditure was highest in West Bengal, while the expenditure on education in that State was lower than that in all other States with the exception of Bihar. Orissa, U.P. and Madhya Pradesh. Bihar and Orissa stood lowest in regard to *per capita* expenditure on education, medical and public health and on social services in general.

Local finance : There are two types of local bodies in India, the municipalities including the large Corporations, and the rural self-governing institutions. Though their sources of revenue are, more or less, common, there is some difference in the relative importance of the different sources in the two types of local bodies. Thus the rural

bodies depend mostly on rates and taxes on land, while the municipalities utilise many other sources like octroi and terminal taxes, besides the taxes on property.

The main sources of revenue at the disposal of local bodies are of two kinds :—tax revenue and non-tax revenue.

The tax revenue is derived from the levy of the following kinds of taxes,—*viz.*, taxes on property, taxes on trade, taxes on persons and fees and licences. Taxes on property are usually of four kinds,—*e.g.*, a tax on buildings and land, cess on lands, and tax on unearned increment in connection with betterment schemes. Of these, the second tax is the main source of income of the district boards. The first, a tax on building and lands, is generally of importance in Bombay, Madhya Pradesh, Madras and West Bengal. The third, betterment taxes, is levied in Madras and Bombay.

Taxes on trade are mostly octroi and terminal taxes. These are levied mainly in Punjab, U.P., Madhya Pradesh and Bombay. District Boards derive some income from ferries in their jurisdictions.

The taxes on persons are the following :—(*a*) a terminal tax on passengers as in Calcutta ; (*b*) a tax on pilgrims levied in Bombay, Bihar, Madhya Pradesh, Madras, Orissa and U.P.; (*c*) taxes on professions, trades and callings levied in Madhya Pradesh, Madras, Punjab, U.P., and West Bengal ; (*d*) taxes on circumstances and property levied in Bihar, Madhya Pradesh, Orissa and U.P.

Fees and licences are numerous as for example, the licence fees for vehicle, dogs and other animals, fees for offensive and dangerous trades etc.

Income from non-tax revenue is derived generally from markets, slaughter houses and rents of buildings and lands owned by the local bodies. This does not of course form an important source of revenue except in some municipalities.

In addition, district boards and to some extent municipalities receive government grants for specific purposes.

The importance of these sources of revenue varies in different States. Thus property taxes are highly important in West Bengal where they formed 47·7 p.c. of the total revenue of the local bodies, followed by Bombay, where they formed 41·6 p.c. of the total revenue of the local bodies. In Punjab and U.P., they formed 4·8 p.c. and

10·5 p.c. of the total revenue of local bodies, whereas octroi and terminal taxes formed 15·1 p.c. in U.P. and in Punjab (13·3 p.c.) Government grants are the most important in Bihar, where they formed 24·07 p.c. of the total revenues of local bodies, followed by Madras (16·6 p.c.) and U.P. (13·4 p.c.) and Punjab (13·3 p.c.). Government grants formed 66·4 p.c. of the total revenues of local bodies in Orissa, 40·4 p.c. in Bihar, 36 p.c. in Punjab and only 5·7 p.c. in Bombay.

The *main heads of expenditure* of the local bodies relate to the following :—general administration, public safety, public health and medical relief, sanitation like drainage, conservancy etc., education mainly primary, and to some extent secondary, public works including the construction and maintenance of roads, bridges, parks, markets and slaughter house etc., expenditure on public health, medical relief and sanitation formed 46 p.c. of the total income of the local bodies in West Bengal, followed by Bihar (39·2 p.c.), Assam (37 p.c.), Bombay (32·4 p.c.). On the whole the *per capita* income and expenditure in the local bodies of India are very low as compared to those of the British local bodies.

The low expenditure is due to the extremely low incomes of these local bodies. The *per capita* income of local bodies in India amounted to only Rs. 1-6-0, as compared to that of Rs. 49-5-0 in the U.K. Moreover, some of the sources of revenue are not free from defects. For example, it is well-known that the octroi duties are highly objectionable. These duties hamper the smooth flow of trade between the rural and urban centres. They fall with inequitable weight on the poor classes. The method causes a good deal of inconvenience to the taxpayers. The octroi, in the words of the late Lord Stamp, "has nearly every vice." It is desirable that these duties should be eliminated altogether in due course. Hence it is necessary to take steps to augment the resources of local bodies and to reform their system of taxation.

Improvement of local finance : That the financial resources at the disposal of local bodies are extremely inadequate is admitted by everybody. What services can a district board with an income of 75 P per head provide for its population? While the resources at their disposal are clearly inadequate, one must also admit that the local bodies have shown an extreme reluctance to make use of their existing financial powers and resources to the fullest extent. There has been

failure to assess taxes with impartially and to collect them promptly. While these defects should be remedied, larger resources must also be placed at the disposal of the local bodies so that they can play an increasing role in the new set-up.

The Local Finance Enquiry Committee of 1951 have suggested that in order to provide local bodies with larger resources, a convention may be established whereby the net proceeds of the following taxes should be exclusively available for the local bodies, *viz.*, terminal taxes on goods and passengers carried by railways, sea or air taxes on lands and buildings, taxes on the consumption or sale of electricity, taxes on advertisements, taxes on vehicles other than those mechanically propelled, taxes on animals and boats, tolls, taxes on professions, trades, callings and employments, capitation taxes on entertainments including amusements and taxes on the entry of goods into a local area for consumption or sale therein. The Committee have also recommended that the present limit of Rs. 250 per person placed on the tax on professions, callings etc., by the new constitution should be raised to Rs. 1,000. The tax on property should be made obligatory and the local fund cess should be raised to 3 as. per rupee. The State governments should also grant a share of the tax on motor vehicle to the local bodies.

It is doubtful how far the State Governments will be able to spare substantial sums for the local bodies by giving more grants-in-aid or by sharing some taxes. The governments themselves are suffering from an inadequacy of funds, and unless substantial sums are made available to the local bodies, it is idle to expect any serious improvement in their working. Local bodies may, however, be authorised and induced to levy taxes on property, and so tap an important source of revenue. Something must also be done to improve the administrative efficiency of the local bodies so that there may not be any under-assessment or accumulation of arrears or any negligence in utilising the existing resources to the maximum extent.

Questions

1. Describe the chief sources of revenue and the main heads of expenditure of the States in India. What suggestions can you offer to ensure a better planning of their revenues and expenditures ?

2. Examine the position of sales tax in the State budgets.

3. Describe the scope and desirability of introducing agricultural income tax in India.

4. What are the main sources of revenue of U.P. Government ? Discuss the position of income tax, sales tax and land revenue in it.

5. Discuss the principal features of State finances in the post-independence era.

6. Briefly describe the main sources of revenue and heads of expenditure of the local bodies in India.

7. Suggest some measures for increasing the revenues of the local bodies.

CHAPTER 42

SOME PROBLEMS OF TAXATION

We have reviewed the main trends in Central and State finances. It remains to discuss the general characteristics of the Indian tax system.

Comments on the tax system : According to the estimates of the Planning Commission, India's total tax revenue formed about 8·5 p.c. of her national income, a very low figure as compared to other relatively advanced countries. Thus the total tax revenue formed 35 p.c. of the national income in the U.K., 22 p.c. in Australia, 27 p.c. in Japan, 23 p.c. in the U.S.A., 27 p.c. in New Zealand, 19 p.c. in Canada and 20 p.c. in Ceylon.

This does not, of course, indicate that the burden of taxation is extremely low as compared to some other countries. The burden of taxation depends on the level of national income of a country, the distribution of that income among the population and other factors. The burden of taxation also depends on how the taxes are raised and spent. The limit of taxation is reached comparatively much earlier in a poor and under-developed country than in a rich and advanced country. So a mere comparison of percentages which taxes bear to the national income does not prove much.

Another striking feature is the relatively small percentage of population affected by taxation in this country. About 28 p.c. of the total tax revenue comes from the direct taxes, excluding land revenue, which is paid mainly by only half of one per cent of the working population of the country. Another 17 p.c., is accounted for by import duties. But the major portion of the yield of these duties is derived from the duties on motor vehicles, motor spirit and oils, high quality tobacco, silk and silk manufactures, liquors and wines etc., which are consumed or used by a relatively small section of the population. A large portion of the yield on the excise duties on tobacco and superfine cotton cloth is also probably paid by a limited number of consumers. It is, of course, true that in a poor country with the vast majority of population living almost on or below the subsistence level, the number of people affected by direct taxation must be narrow. This fact that only a small section of the people is affected by taxation is responsible for

the relatively small proportion of the national income being absorbed by taxation. It also accounts partly for the fact that the existing level of taxation appears to be heavy.

In view of these considerations it has been urged that in this country increasing reliance would have to be placed on indirect taxes in raising the required revenue. As the scope of direct taxation is limited, the incomes of the greater part of the population can only be reached through the taxes on commodities. Moreover, the rates of income tax are already too high for an under-developed country like India, and there is little scope for raising more revenue through direct taxes. On the other hand, it may be necessary to give some relief to the income tax payees in order that the burden of this tax falls with less rigour on initiative, enterprise and saving.

While there may be some truth in this contention, one must also remember that the taxes on commodities are usually highly regressive. There is already a strong feeling that the burden of taxation in this country does not fall equitably on all sections of the population. Hitherto taxes have been levied to meet the annual needs of the budget rather than on any planned basis. The war and post-war inflation and the comparative inelasticity of the land revenue have served to reduce the burden on the agricultural classes and on some sections of the industrial workers. On the other hand, the burden on the middle income groups has increased considerably.

A system of taxation has to be judged not only in relation to the amount of taxes raised, but also with respect to the way in which the revenue is being spent. Tax rates may be heavy, but if the proceeds are utilised in providing welfare expenditure for the tax-payers, the burden is to that extent minimised. In the Indian tax system, as we know, the major portion of revenues raised by both the Union and the State Government is spent on security services, and only a comparatively small portion is utilised for the provision of social services. It is of course true that in the last few years the proportion of the total revenues spent on social services has been increased to some extent. We have yet to travel a long way on the road to social security.

The tax system and inequality of incomes : Neither is the present tax system contributing very much towards the reduction in the inequality of incomes so widely prevalent in the country. The major portion of

the total revenues is raised through indirect taxes, and the increased yield from the union excise duties implies a relatively greater burden on the middle and poorer sections than on the comparatively rich. It is well-known that in India one finds wide divergences in money incomes, extremes of poverty to be found existing side by side with a great deal of "conspicuous expenditure." The rates of income tax are of course high, especially on very large incomes. But on account of administrative inefficiency and corruption, there is large-scale evasion in both large and middle income groups. Repeated attempts to seek out these hiddlen incomes have met with comparatively little success. As a result, the income tax is not effective in reducing the inequality of incomes to a significant extent in spite of the high rates. The estate duty has only recently been levied, and the country has yet to feel the impact of this levy. The increasing importance of the sales tax in the State revenues has only served to increase the regressive character of the tax system. There have been only feeble attempts to tax luxuries at higher rates, and necessaries have not always been exempted from this tax. A considerable portion of the yield from import duties comes, no doubt, from luxury articles. But other articles of import are also being taxed at higher rates, and to that extent these duties are proving to be regressive.

As has already been pointed out, the pattern of public expenditure does not also provide any ground for the belief that it was an important factor in the reduction of inequality of incomes. This will not be the case unless a larger proportion of the public revenues is spent on the provision of old age pensions, sickness and unemployment insurance and other measures of social security.

A point regarding the increasing public expenditure should also be noted. Since the advent of independence there has been a tendency to multiply the number of posts in the government service at higher levels. For example, the present territory of West Bengal comprises one-third of the area of undivided Bengal. Whereas the administration of Bengal was managed by a small number of ministers, the present truncated area of West Bengal has in all 18 or 19 Ministers to look after its administration. There have been too many joint secretaries, additional secretaries and the like, making the civil administration rather top-heavy. The bureaucracy has a natural tendency to multiply itself, and it is absolutely essential to keep a strict

watch over this process. It is common knowledge that a very large number of new posts have been created during the last few years. There has been expansion of the Central as also the State Secretariats in almost all grades of offices. These new additions have proved to be a source of conflict between ambitious officials of different departments in seeking control over particular projects or measures. There is, therefore, a great need for the practice of economy in almost all Government Departments so that the savings thus made may be diverted towards developmental and welfare expenditure.

There are several ways in which the tax system can be improved. In the first place, as the people get accustomed to the estate duty, the rates of duty could be raised and the exemption limit lowered so as to collect more revenues from these sources and at the same time to reduce the present inequality in the distribution of wealth. Secondly, a reform of income tax administration should be aimed at and a determined attempt should be made to stop all loopholes and to prevent large-scale evasion of taxation. Thirdly, the structure of the sales tax should be made progressive by levying this tax on luxuries at considerably higher rates. Some uniformity in the rates of sales tax as between the different States should also be our aim. Fourthly, as the Planning Commission has suggested, land can now bear a higher share of the tax burden. The different State Governments should adopt betterment taxes. The rates of agricultural income tax should be steepened. Lastly, taxes on capital gains, and on windfalls should also be made a part of the tax structure of this country. These measures would not only provide more revenues to meet the development expenditure, but would also result in some reduction in the inequality of incomes.

Kaldor's tax reform proposals : In 1956, the Government of India invited Mr. N. Kaldor of the Cambridge University to suggest changes in the Indian tax system so that sufficient revenues could be raised for the Second Plan. Mr. Kaldor confined himself mainly to the field of direct taxation and made in his report a number of interesting suggestions for the reforms of the direct taxes. He suggested, first of all, the introduction of an expenditure tax, as a partial substitute for the super tax on income, the levy of an annual tax on wealth, the levy of a gift tax, and finally, a capital gains tax. The taxpayers were to submit a comprehensive annual tax of their income and wealth, including annual accretions to wealth. From this it would be easy

to determine their expenditure, and the tax on expenditure should be levied on a progressive basis. As a counter-vailing measure, the maximum rate of tax on personal incomes was to be reduced to 7 as. in the rupee. This step, together with the expenditure tax, would provide enough incentive to saving. To compensate for the consequent loss of revenue, an annual tax on wealth varying from $^1/_3$ p.c. to $1\frac{1}{2}$ p.c., another tax on gifts and on capital gains were to be levied. These taxes would bring in sufficient revenue without exercising any disincentive effects on saving and enterprise. A similar reform was also to be carried out in the sphere of corporate taxation. Profits of companies were to be taxed at the rate of 45 p.c. per rupee, and all other direct taxes on business were to be repealed. To deal with the question of evasion of direct taxes, he recommended that the law should provide for the compulsory auditing of all accounts of income in excess of Rs. 50,000 in the case of income from business and Rs. 1,00,000 in the case of personal incomes.

The four Kaldor proposals—expenditure tax, capital gains tax, wealth tax and the gift tax have been introduced into the Indian tax system in subsequent years, of course in a much modified form. But the introduction of these measures had not been accompanied by the suggested reduction in personal as well as the corporate rates of taxation. So it was not possible to test his hypotheses regarding saving and enterprise. In particular, the expenditure tax has been a highly controversial tax. In the Indian context it as well as the wealth and the gift taxes have not proved to be remunerative. It did not matter much if they were repealed or retained. There was doubt whether their combined yield would have compensated for the loss of revenue that would have taken place with the suggested reduction in the individual and corporate tax rates.

Questions

1. Describe whether the Indian tax system is just in its incidence on different classes of people.

2. What are the principal defects of the Indian tax system ? How can they be best remedied ?

3. Discuss the Indian tax structure as to its effectiveness in reducing inequalities of wealth and income.

4. Comment on the existing tax structure of India. What changes will you like to make in it with a view (*a*) to making it more progressive, and (*b*) ensuring greater revenue for developmental purposes ?

5. "The Indian tax system is regressive." Examine this statement. (C. U. B.Com. 1957).

CHAPTER 43 THE UNEMPLOYMENT PROBLEM

Introduction : Of late the problem of growing unemployment has attracted public attention. It should, however, be borne in mind that unemployment had always been present in our economy. In fact, unemployment is often a characteristic of under-developed economies. As at the present moment public mind also became considerably agitated over the growth of unemployment in the twenties of this century. A number of provincial governments appointed committees to assess the magnitude of the problem and to suggest proper remedies. In particulr, the problem of middle class unemployment became very acute in these years, though there was also considerable unemployment among the industrial workers. The outbreak of the second world war provided a partial solution of the problem in all its different aspects and with the increase in the tempo of the war this country reached almost the state of full employment. Employment increased both in the organised and small-scale industries. During the fifties the problem has again tended to become acute.

Extent of unemployment : There are unfortunately no reliable statistics to assess the volume of unemployment in the country. A number of studies have been made to secure reliable information on the subject. One important source is furnished by the data available from the Employment Exchanges. Thus the total number of persons registered on these Exchanges has increased from 493,000 in July, 1953 to 589,000 in July, 1954, an increase of about 20 p.c. During the same period, the number of persons seeking clerical and other white-collar jobs increased from 155,000 to 198,000 a rise nearly 28 per cent. These data do not, of course, provide any reliable guide as to the exact volume of unemployment. It may, for example, be likely that greater use is being made of these Exchanges by persons seeking jobs in recent months than was the case in earlier years. Moreover, there are some persons who are already employed, but are seeking better employment through the Exchanges. On the other hand, there is also no doubt that quite a considerable number of unemployed people have not taken the trouble of registering themselves at the Exchanges as the latter have succeeded in placing men in jobs only

in a small percentage of cases. Taking all these factors into consideration, there can be no doubt that there is an upward trend in unemployment in the urban areas, particular among the educated, middle-income groups.

There are also other evidences of growing unemployment collected by various surveys. Thus a survey conducted in the city of Calcutta showed that about 7 p.c. of the total working population of the city was found unemployed, and about one-half of the unemployed belong to the educated middle classes. Another survey in Travancore-Cochin revealed that 22 per cent of males and 64 per cent of women were unemployed, and that the incidence of unemployment was the highest among the middle classes. There are, moreover, signs of some amount of unemployment among the industrial workers, especially after the mild recession in prices which took place in early 1966. For example, a survey conducted by the Bureau of Economics and Statistics of Bombay State showed that of the total labour force about 1·2 per cent among the male workers and a small number of women and children were unemployed. As yet, however, the problem is not very acute among the rural population there have always been considerable unemployment and under-employment. For example, the Travancore-Cochin survey showed that though the incidence of unemployment was greater in the urban areas, it was none-the-less almost equally serious in the rural areas. There has always been a large surplus population on the land, only partially employed.

There is no doubt that the increased expenditure under the Plan is also making an appreciable contribution to the enlargement of employment opportunities, especially in areas where the large River Projects and other development schemes are going forward. Thus while unemployment is growing, employment is also expanding. The fact is that the tempo of development which has so far been planned has not led to the creation of new jobs at a rate fast enough to absorb the additions to the number of job-seekers of about 1·5 million per year that accompany the increase in population.

Causes : The most important factor leading to the rise in unemployment is the pressure of population relative to the growth in the volume of capital equipment in the country. As has already been pointed out, the planned expenditure has not created a sufficient number of jobs to absorb the increase in population that is now taking

place both by birth and migration. The large volume of unemployment in Calcutta, for example, may be stated to be due to some extent to the large-scale migration of population from East Bengal, following the partition of the country. The large influx of population has naturally led to growing disparity between the number of available jobs and that of job-seekers.

The situation was aggravated by the onset of business recession in the early part of 1966. This has led to the contraction in employment provided by the businessmen, especially for the white-collar jobs. It has also been responsible for a much slower rate of increase in the volume of employment in certain other directions.

Part of the educated middle class unemployment may be due to the growing imbalance between the number of available white-collar jobs and the large number of educated people turned out by our universities and schools. The education provided by the universities makes the students fit for only the clerical and similar types of jobs. The social conventions among certain sections of population generate a feeling of contempt for manual labour with the result that the so-called Bhadraloks seek only the white-collar jobs, which are supposed to preserve their respectability.

The growing rural unemployment has been due principally to the pressure of population on the limited supplies of land, coupled with the decay of most of the village industries in the face of machine competition.

While these factors are important, especially in influencing the volume of different types of unemployment, one must remember that unemployment has often been caused by the structural imbalance to be found in most of the under-developed areas. Such economies are in most cases characterised by a surplus population and a low rate of capital formation. The result is inevitably unemployment and under-employment.

Remedies : The growing volume of unemployment caused great concern in the country, and various suggestions were made to increase the volume of employment. The Planning Commission enlarged the scope of the First Plan by increasing the total outlay, and an 11-point programme was adopted in order to augment the employment-potential of the Plan. The Ministry of Education adopted a special programme

for the expansion of education in order to provide employment for the educated unemployed.

The impact of these measures has not been large. In a recent debate in the Loksabha the Finance Minister has stated that "the central objective of our economic policy from now on must be to create full employment conditions within a measurable period, say, ten years from now." This means that measures would have to be taken to create at least two million new jobs, if not more, every year, and these jobs must obviously be created in the non-agricultural sector. After taking into account of the normal rate of growth in employment, it would mean the creation of a total of about 24 million jobs to achieve the target of full employment. Out of this 12 million jobs are to be found at the end of the Second Five Year Plan. To achieve this target it would be necessary to invest about Rs. 1,000 crores annually. In future plans special attention would have to be paid to the development of small-scale industries in view of the paucity of capital in the country.

The remedies are to be divided into two groups, short-period remedies and long-term ones. Short-period remedies should aim at providing immediate solutions for the problem of unemployment. The government should concentrate attention on the adoption of measures designed to result in an increase in the volume of employment within a short period of time, instead of concentrating mainly on long-term measures as was the case in drawing up the First Five Year Plan. The First Five Year Plan was defective from this point of view. While it is necessary that we should adopt measures for bringing about structural changes in the economy, and removing the main deficiencies like food-shortage, some attention should also be paid to the need of securing an expansion in the volume of employment. And as far as possible, these short-term measures should be directed towards those areas or sections of population where the impact of unemployment is the greatest. The provision of more employment is the greatest. The provision of more employment in the urban areas should, therefore, be one of the central aims in the framing of our Five-year plans.

The long-term measures should aim at (*a*) securing an economic organisation which would be labour-intensive, rather than capital-intensive, and (*b*) re-organising and improving the system of education so as to remove the present wastage. The reform of the educational system should remove the present lop-sided characteristic of the

employment market, where a large number of students come out every year for jobs with practically no special qualifications except a smattering of some general information. It should aim at providing increasing facilities for the training up of those types of skilled personnel of which there is now considerable shortage,—a shortage which is often hampering development in many directions. The development of certain essential heavy industries should, of course, be pushed through. But more and more attention is to be paid to the task of encouraging the growth and development of small-scale and medium-sized industries, which use more labour per unit of capital. There is no reason why an under-developed, over-populated country like India should pursue the same path of industrialisation as was to be found in the U.S.A., or the U.K. We should make experiments to evolve another type of economic system, which can prove equally efficient, though based mainly on small-scale and medium-sized industrial units. Research on the evolution of suitable techniques should be undertaken.

Lastly, some attention should be paid to the task of controlling the rate of growth of population in the future. The spread of education, the emancipation of women and the kindling of a desire for a higher standard of living are no doubt expected to lead to a decline in the birth rate as has been the case in the western countries. What is now wanted is to expedite the movement by the adoption of measures designed to make the knowledge about birth control available to everybody, or at least to those who would like to restrain the rate of birth in their families. Those who seek such knowledge should not have any difficulty in getting it. If this is done, the inexorable march of events would gradually lead to a decline in the rate of growth of population.

Unemployment is a hydro-headed monster, and the modern state has no alternative but to fight it out on all fronts with a large variety of weapons. We must evolve an economic system guaranteeing jobs for everybody seriously seeking employment, and we must at the same time adopt measures for raising the standard of living of every individual in the country. It is, of course, true that this is not the task of the economist alone. The scientist, the educationist, the social reformer and many others should also make their contributions towards this goal of building up a happy and prosperous India. But the economist has an important part to play. He should seek facts on which to base policy-decisions, probe and analyse them, and try to draw correct conclusions.

Questions

1. Examine the causes and extent of unemployment existing at present in this country. What provisions have been made in the Third Five Year Plan to solve this problem ?

2. What measures would you advocate for solving the present-day problem of unemployment in India ?

3. Examine the causes of the recent increase in unemployment in India. How far would the Second Five Year Plan help to solve the problem ? (C. U. B. Com. 1957).

CHAPTER 44 THE FIRST FIVE YEAR PLAN

This is the age of planning, and a number of countries have formed plans for the development of their economic resources. The term, economic planning, refers to the plans formed by a central authority for the systematic and balanced development of the productive resources of a country with a view to raising the national income or to achieve some other purpose. An economic plan is so designed as to secure larger and balanced production of goods and better distribution of incomes than is usually the case under the unplanned economy of modern times. Under the system of individualistic economy, there is no organisation for the conscious direction of the processes of production. Such unplanned economic development has often given rise to a number of evils. It may lead to the over-production of certain types of goods and under-production of others. As the productive system is geared to meet the demand of the richer classes, a large part of the investment may be directed to the production of luxury articles to the neglect of essential commodities. There is, moreover, a serious inequality of incomes and wealth, as a result of which extremes of poverty and wealth are found side by side. The method of economic planning seeks to avoid these defects. The object of an economic plan is to increase the level of production by developing resources which are usually left untouched or under-developed by private enterprise. It aims at securing a better distribution of investment and at a more balanced growth of production of various types of goods.

The necessity for forming an economic plan for the development of the resources of India has been felt from a long time. India is an extremely poor, under-developed country, possessing large resources awaiting development. Conditions in this country are almost similar to those which prevailed in Soviet Russia before that country started on its career of economic planning. There is no reason why we should not be able to increase the standard of living of the people if an attempt is made to develop the resources on the basis of a well-conceived economic plan. This was pointed out in 1931 by Sir Arthur Salter, who was asked to conduct an enquiry into the economic conditions of India. Again in 1935, Dr. Bowley and Prof. D. H. Roberton pointed out the need for formulating an economic plan in this country. In 1938, the President

of the Indian National Congress, Shri Subhas Chandra Bose, set up a committee under the Chairmanship of Shri Jawaharlal Nehru for framing an economic plan for this country. The National Planning Committee, as it was known, collected valuable materials, but its work was interrupted on account of the arrest of the important Congress members.

The first definite economic plan that was framed was the *Bombay Plan,* drawn up by eight leading industrialists of India. This plan aimed at doubling the *per capita incomes* within the next 15 years at a total investment of Rs. 10,000 crores. The emphasis was mainly on industrial development, the development of agriculture being given the second priority. Next came the *People's Plan* framed by the late M. N. Roy and his group. This plan sought to invest Rs. 15,000 over the next 10 years. The *Gandhian Plan* was formed by Shri S. N. Agarwala of Wardha. It sought to develop a decentralised economic system, laying greater emphasis on the development of agriculture and small-scale industries at an estimated cost of Rs. 3,500 crores.

The Government of India also set up a committee for this purpose, and later issued the Second Report on Reconstruction Planning for the purpose of formulating an economic plan. After the achievement of independence, the government became serious, and appointed the Planning Commission in 1950 for drawing up an economic plan for this country. The Commission published a draft Five-Year Plan in 1951 for discussion and criticism. Finally, the Five-Year Plan was published in December, 1952.

The First Five-Year Plan : The Planning Commission submitted a Draft Plan in July, 1951. The Plan was to cover the period, April, 1951 to March, 1956. It was divided into two parts. The first part involved an expenditure of Rs. 1,493 crores, and consisted largely of projects already in execution in different parts of the country. The second part proposed an additional expenditure of Rs. 300 crores, which was to be incurred only if external assistance was forthcoming.

The final Plan was published in December, 1952. It proposed to cover the same five-year period as in the Draft Plan. But unlike the Draft Plan it was not divided into two parts. It was an integrated single Plan, and it provided for a larger sum of outlay, while retaining the main pattern of outlay as far as possible. We propose to summarise the main provisions of the Plan in the first place, reserving a discussion of its basic features later on.

Summary :—The Plan proposed a total outlay of Rs. 2,069 crores over the period, 1951-56, by the public authorities. The distribution of this total expenditure on different sectors is summarised in the following table.

TABLE I

Name	(Rs. Crores)	Per cent of the total
Agriculture and Community Development ..	361	17·5
Irrigation	168	8·1
Multi-purpose Irrigation and Power Projects	266	12·9
Power	127	6·1
Transport and Communication ..	497	24·0
Industry	173	8·4
Social services	340	16·4
Rehabilitation	85	4·1
Others	52	2·5
	2.069	100·0

In addition to provision of this amount of expenditure, the Plan fixed targets of production to be achieved in different sectors of the economy. Table II summarises the targets to be achieved in main lines of production as compared with those at the beginning of the Plan (*i.e.*, in 1950-51).

TABLE II

	1950-51	1955-56
I. *Agriculture*		
Foodgrains (million tons)	52·7	61·6
Cotton (lakh bales)	29·7	42·2
Jute ,, ...	33·0	53·9
Sugarcane (million tons)	5·6	6·3
II. *Irrigation and Power*		
Irrigation (million acres)	50·0	69·7
Electrical energy (installed capacity in million k. w. s.)	2·3	3·5

III. *Industry*

Pig iron available for foundries (lakh tons)	3·5	6·6
Finished steel (lakh tons) ..	9·8	13·7
Cement (lakh tons)	26·9	48·0
Cotton yarn (million lbs.) ..	1179	1640
Mill cloth (million pds.)	3718	4700
Handloom cloth (million yds.) ..	816	1700
Jute manufactures (thousand tons) ..	892	1200
Bicycles (thousands)	101·0	530·0
Power alcohol (million gallons) ..	4·7	18·0

IV. *Transport*

Shipping (tonnage)		
Coastal (GRT thousands) ..	211·0	315·0
Overseas (GRT thousands) ..	173·5	287·0
Roads :—		
National highways (thousand miles)	11·9	12·5
State roads (thousand miles) ..	17·6	20·6

In addition, there were to be increases in the number of hospitals, dispensaries, primary schools, secondary, basic and industrial schools, other technical and vocational training schools, Panchayats and Co-operative societies.

Lastly, the Plan proposed to devote a small sum of money to experiment upon, and popularise different systems of family planning with the object of controlling the growth of population.

As for the resources for financing the Plan, the Planning Commission estimated that about Rs. 378 crores would be available from the budgetary surpluses of the Central and State Governments after meeting their non-development expenditure. The Governments would be able to raise Rs. 520 crores through loans from the public, small savings, deposits and other funds etc. In other words, this sum would be raised from private savings. Thus budgetary surpluses and private savings would meet about Rs. 1,258 crores of the planned outlay of Rs. 2,069 crores. External assistance amounting to Rs. 156 crores has already been received or promised from the International Bank, the U.S.A.,

Canada, Australia, New Zealand and other countries. The total thus amounted to Rs. 1,414 crores. This left a gap of Rs. 655 crores. "This gap has to be met from further external resources, or in the absence of it, by additional measures of internal taxation and borrowing and from deficit financing."

What has expected to be the impact of the Plan on the national income of the country ? According to the Planning Commission, the national incomes of India in 1950-51 had been estimated at Rs. 9,000 crores. If the Plan was fully implemented, the national income would rise to Rs. 10,000 crores in 1955-56, *i.e.*, an increase of 11 per cent over the whole period. But the benefits of the outlays on various projects of investment undertaken during the Plan period would not however, be fully realised in this period. Out of this annual rate of increase of about 2 per cent in national income, about one-fifth would have to be ploughed back into investment in order to finance the development programme laid down in the Plan. The aggregate consumption expenditure would, therefore, rise at a somewhat lower rate than the national income. Thus the Plan would not actually mean any material improvement in the economic conditions of the people. But "it will have made a substantial addition to the production potential of the country." The Plan was, moreover, one of a series, which, when completed, were expected to double the national income after 27 years.

The Plan and Agriculture : The first Plan gave the highest priority to the development of agriculture. Thus out of a total of Rs. 2,069 crores, Rs. 361 crores were to be spent on agriculture and community development and Rs. 168 crores in irrigation. Thus in all Rs. 529 crores or 25·6 p.c. of the total would be spent on the development of agriculture. The various multi-purpose irrigation and power projects on which Rs. 266 crores or 12·9 p.c. of the total would be spent would also contribute greatly to the development of agriculture through the provision of increased irrigation facilities and generation of electrical energy. Recognising that the problem of agricultural development was mainly one of adequate water supply, the plan had given great emphasis to the construction of irrigation works. Thus about 21 p.c. of the total expenditure had been allotted for irrigation, and when all the projected irrigation works were completed the total irrigated area would increase from 50 m. acres to 69·7 m. acres in 1956.

Besides these provisions for irrigation the Plan had also laid down a proper land policy designed to secure an increase in agricultural production. Thus the Plan recommended the abolition of zemindari and other intermediate interests. After these intermediary interests were abolished, land would be left in the hands of large owner-cum-cultivators, small and middle owner, tenants-at-will and landless workers. As the majority of large owners do not usually cultivate their land, it was desirable to fix an upper limit to the amount of land which an individual might hold, in order to prevent the formation of very large holdings and to secure a more equitable distribution of land. As regards the small and medium owners, the general aim should be to encourage them to form co-operative farms. Every State should have a programme for the consolidation of holdings and it should fix a minimum holding below which sub-division was not to be permitted. Tenants-at-will should ordinarily hold tenancies for periods varying from 5 to 10 years. In fixing the rent of land regard must be paid to the fact that the cultivators received at least fair wages for their labour. A rate of rent in excess of one-fourth or one-fifth of the produce should not usually be allowed.

In addition to land reforms, the Commission's proposals embraced the construction of more minor and major irrigation works, reclamation and intensive farming based on the application of the results of research. Much reliance was to be placed on the method of co-operative village management, and on Community Development Projects and Rural Extension Schemes to bring about an integrated, all-round improvement in the social, economic and educational standards of the rural population. In addition, the Commission made detailed references to the reform of the machinery for providing agricultural finance, improved marketing organisation for crops, to a better system of animal husbandry, dairying and horticulture, increase in the forest areas and soil conservation, and lastly, to the necessity of developing and exploiting the fisheries.

When all these proposals were fully implemented, there would be increased production of foodgrains by about 14 p.c. There would also be sizable increases in the production of commercial crops, and the Plan includes targets of production to be achieved in respect of these crops.

This is an outline of the main proposals which had been made in the Plan with respect to agriculture. While there might be

difference of opinion in respect to some of the detailed proposals for improvement of agriculture, these were not, after all, so important as the central question, whether the high priority given to agriculture was justified or not. The Commission adduced several reasons to justify the high priority to agriculture in the Plan. First, the economic organisation of this country was based predominantly on agriculture, which provided the main occupation for about 70 p.c. of the total population. Agriculture was, therefore, a basic and vital industry in this country. This important base must be strengthened and improved before one proceeded to create a vast super-structure over it. Secondly, without a substantial increase in the production of foodgrains, the effective operation of the Plan could be ensured. "Foodgrains occupy a pivotal place in the price structure because if their prices rise, this leads directly to the rise in the cost of living and in production costs all round." Lastly, unless a sizable surplus has created somewhere in the economy. it would not be possible to increase the pace of investment for the purpose of raising the national income. In view of the extremely low yield in agriculture, it would be comparatively easier to create a surplus in the agricultural sector as compared to industries or other sectors of the economy.

These were certainly weighty arguments. But it has been urged that a Plan should aim at securing a well-balanced economy. The Indian economy was, however, ill-balanced, with excessive predominance of agriculture and comparatively small development of other sectors. The Plan should aim at curing this unabalanced growth by giving less attention to agriculture and more to industries. Secondly, it was stated that the possibilities of creating a surplus did not lie only in the agricultural sector. They also existed in the industrial sector, where many gaps were to be found such as the lack of a machine manufacturing industry etc. If these gaps were filled up. a great advance in the development of our economy could be secured.

It is of course true that the Indian economy was ill-balanced, and that other sectors should be developed to remedy this situation. But the high priority given in the Plan to agriculture might be defeated on the ground that this paved the way to the development of other sectors. One should not forget that much of the expenditure on agriculture would ultimately facilitate industrial development. For example, the completion of the multi-purpose projects would not only benefit agriculture,

but would also lead to the generation of cheap electricity, and this would foster industrial development in the next round. Secondly, increased production of industrial raw materials would go a long way to solve the problems of industries, and the availability of increased quantities of food grains at lower prices would keep down cost of living. and would thus take away the basis for the demand for increased wages, which as the industrialists claim, is now standing in the way of industrial development. The development of agriculture was thus designed to carry us a step further towards industrial development.

The Plan and industries : Of the total outlay of Rs. 2069 crores, 8·8 per cent or Rs. 173 crores would be devoted to the expansion of industries in the public sector. This was an improvement upon the Draft Five Year Plan where it was proposed to spend Rs. 101 crores or 6·7 per cent of the total expenditure on industrial development.

In addition to this expenditure, private enterprise was expected to spend Rs. 233 crores on the development of industries. A further sum of Rs. 150 crores would be necessary for replacement and modernisation of plant and machinery. After taking into account the requirements for working capital and some other items of expenditure a total sum of Rs. 707 crores was to be spent on the development of industries both in the public and private sectors.

The Commission fixed the following order of priorities for the development of industries. The highest priority was to be given to the expansion of productive capacity in capital and producer goods industries like iron and steel, aluminium, cement, fertilisers, heavy chemicals, machine tools etc. Secondly, with respect to major consumption goods industries like cotton textiles, sugar, soap, vanaspati, paints and varnishes, the aim should be the fuller utilisation of existing capacity rather than the establishment of new units. In the opinion of the Commission the existing capacity in these industries is adequate for present requirements, and the emphasis must be on increasing the efficiency and output of existing plants. Thirdly, new plants were to be set up in those lines of production, which would lend strength to the industrial structure by rectifying as far as resources permitted the existing lacunae and drawbacks. Lastly, industrial units on which a part of the capital expenditure had already been incurred were to be completed.

In the public sector the major industrial project was a new iron and steel plant estimated to cost Rs. 80 crores in all. The plan also provided for the completion of the Chittaranjan Locomotive Factory at Mihijam and of the machine tool factory in Mysore, and for the expansion of the Sindri Fertiliser Factory and the development of the Vishakapatnam shipping yard. In the private sector, about 80 per cent of the total outlay was in respect of capital goods and producer goods industries such as the iron and steel industry (Rs. 43 crores), petroleum refineries (Rs. 64 crores), cement (Rs. 15·4 crores), aluminium (Rs. 9 crores). and fertilisers, heavy chemicals and power alcohol (Rs. 12 crores). Taking both the public and private sectors together, about 26 per cent of the total investment would be in respect of metallurgical industries, 20 p.c. into petroleum refining, 16 p.c., into engineering industries and 8 p.c. into the manufacture of heavy chemicals, fertilisers and pharmaceuticals.

In the matter of industrial development, the main reliance was placed upon private enterprise. The Planning Commission has published a list of 42 industries in which further development or expansion is considered desirable. If private enterprise carries out the plan as desired, substantial increases in output would be achieved in respect of the consumer goods and producer goods industries.

TABLE III

Name	Increase in output
Cloth	1,872 million yds.
Sugar	384 thousand tons.
Salt	429 ,,
Paper and Paper Board	86 ,,
Vegetable Oils	182 ,,
Iron and Steel	310 ,,
Pig Iron	394 ,,
Finished Steel	2,108 ,,
Cement	83 ,,
Aluminium	156 ,,
Heavy Chemicals	150 ,,
Locomotives	(+50 boilers)
Diesel Engines	4,45,000

Increases were also expected in respect of durable consumer goods like bicycles, sewing machines, antibiotics, power driven pumps etc.

This was certainly not an ambitious programme for securing a rapid development of industries. The Commission's justification for such a modest plan for the expansion of industries lay in the fact that in view of the limited resources and savings, it was not possible to devote a larger sum to industries after spending so much on the development of agriculture and irrigation. Larger allocation for industries would have meant either more resort to deficit financing or the imposition of more austerity on the people. Either course would be undesirable.

Since the development of industries was to be left mainly to private enterprise, much would depend on the extent to which it functions in relation to the Plan. Two questions were involved in this matter. Would private enterprise be able to raise the necessary finance for carrying out the task allotted to it ? And would private enterprise move into the industries whose development was desired by the Plan ? The Progress Report of the Plan had however shown that private enterprise had responded to the desired degree in fulfilling its quota under the Plan. In spite of the present state of the capital market. private enterprise was able to raise the necessary finance from the market or from its own resources, after the Government borrowed the funds. Moreover, in the private sector, the Government could only influence, but it could not determine the actual course of investment Assuming that private enterprise was able to raise the necessary finance, it would naturally tend to invest in those industries, where the chances of earning profits were the maximum. There was no certainty that it would of itself move into the 42 industries whose development was included in the Plan.

The Plan and employment : It has been a serious criticism of the Plan that it had not been framed for the purpose of ensuring full employment in the country. The Planning Commission gave some thought to the relationship between the Plan and the volume of employment. It expected that the Plan would make a two-fold contribution to the solution of the problem of unemployment. Firstly, in the process of increasing the volume of investment it would provide more employment for those engaged in construction activity. Secondly, by building up capital at key points in the system, the Plan would provide a larger number of people with employment at the next stage. According

to its estimate, the Plan would provide additional employment for about 5½ million people and part-time employment for another 3½ million people. This would of course touch the fringe of the problem as according to rough estimates the number of unemployed or under-employed people amounted to about 165 million. Conscious of the small contribution the Plan would make towards the problem of unemployment, the Planning Commission justified its course by pointing attention to the fact that "the elimination of unemployment in an underdeveloped economy is by its nature a somewhat long-term problem,. . . . Expansion of employment opportunities is, in the last analysis, a function of the rate at which national output is being raised, and it is for this reason that a plan of development for a particular period has to be viewed as part of a bigger programme on an accelerated rate."

Within two years of the start of the Plan, the pressure of growing unemployment forced the government to devise measures for the relief of unemployment. The Planning Commission had to give attention to the consideration of short-term measures for providing more jobs for the people. The result was the adoption of the eleven-point programme by the Commission. The programme provided for (*a*) the establishment of work and training camps in places where additional construction is proceeding, *i.e.*, in irrigation and power projects, road construction programmes, co-operative land settlement projects etc.; (*b*) the grant of special assistance to individuals and groups of individuals for establishing small industries and businesses ; (*c*) active encouragement to be given to the products of cottage and small-scale industries through the purchase of stores required by State Governments and public authorities ; (*d*) the expansion of training facilities in these lines where man-power shortage existed at the present moment ; (*e*) opening of one-teacher schools in the rural areas and the establishment of adult education centres in urban areas ; (*f*) establishment of the National Extension Service in the rural areas ; (*g*) development of road transport ; (*h*) encouragement of private building activities ; (i) implementation of slum clearance schemes and programmes for the construction of houses for low-income groups in urban areas ; (*j*) planned assistance to refuge townships and (*k*) encouragement of schemes for the development of power sponsored by private capital.

New schemes designed to relieve unemployment at an additional expenditure of Rs. 150 to Rs. 175 crores were embodied in the Plan.

The impact of these schemes on the volume of unemployment in the country was problematical. The problem was complicated by the fact that with the spread of education the schools and colleges were turning out every year large numbers of pupils, who sought to enter the employment market. The temporary recession in business, following the fall in prices which took place in the early months of 1952, had also affected the employment situation adversely. A re-orientation of the Plan was necessary in the direction of provision of more employment opportunities while maintaining the basic structure of development. The problem of unemployment is a complicated one and would have to be attacked on all fronts.

The financing of the Plan : The Plan proposed to spend a total sum of Rs. 2,069 crores in course of the next five years. How had the Commission proposed to raise the sum ? Table IV summarises the sources from which the Commission expected to raise the required sum.

TABLE IV

Plan Period 1951-56 (Crores of Rupees)

	Centre (including Part C States)	Part A and B States	Total
(1) Public Savings from :—			
(a) Current revenues	160	408	568
(b) Railways	170	—	170
(2) Private Savings from :—			
(a) Loans from the public	36	79	115
(b) Small Savings and other unfunded debts	270	—	270
(c) Deposits, funds and other miscellaneous sources	90	45	153
Total of (1) and (2)	726	532	1,258
(3) External aid received			156
			1,414
Gap			655
Total of (1), (2) and (3)			2,069

With the expanded outlay of Rs. 2,244 crores, the gap was likely to be larger by another Rs. 310 crores, made up of Rs. 175 crores on account of the additional outlay and of Rs. 135 crores on account of the estimated shortages in the budgetary resources of the Central and the State Governments over the five-year period. The Commission estimated that during the period of the Plan, India would be able to draw upon its sterling balances to the extent of Rs. 290 crores. So the extent to which these balances would be utilised, it would add to the total resources available in the country either for consumption or for investment or for both. The gap in excess of this amount had to be met from further external resources if available, or in the absence of it, by additional measures of internal taxation and borrowing and from deficit financing.

The Plan was criticised on the ground that its estimates of available financial resources were rather too optimistic. As regards public savings, both the Central and the State Governments failed to raise the necessary budgetary surpluses. The State Governments in particular fought shy of imposing betterment levies and higher irrigation rates. Hence they failed to raise the necessary budgetary surpluses in addition to their normal non-developmental expenditure. The amount of foreign assistance had of course been larger, amounting to about Rs. 232 crores up to the end of April, 1954. But this was clearly inadequate to meet the gap in the estimates.

There was no escape from the conclusion that greater recourse to deficit financing would be necessary if the target of expenditure set in the revised plan was to be achieved in the period covered by the Plan.

Deficit financing : The term, 'deficit financing', is applied to the case when a government, faced with the excess of expenditure over its receipts from all sources, meets the resulting deficit either by issuing currency, or by borrowing from the Central Bank. When a government finds that its total receipts fall short of its total expenditures, both on revenue and capital accounts, it may seek to raise additional loans from the public. If these prove insufficient, it has either to run down its previously accumulated cash balances, or borrow from the Central Bank or issue new paper currency notes. In all these cases, the total volume of money in circulation tends to rise in the country. These measures will then have an inflationary effect on the economy. If these things

occur during a depression, the increased supply of money will probably lead to the absorption of the unemployed factors into employment and the production of more goods. So deficit-financing may be followed by no or insignificant rise in prices until the stage of full employment or near—full employment is reached. To that extent deficit-financing may be regarded as a pardonable departure from the strict code of financial ethics. Thus it is a helpful device and a valuable instrument in promoting economic development in an under-developed country. But extreme caution may be necessary when using this method financing economic development lest inflation should get out of hand. Like fire, deficit-financing is a good servant, but a mad master.

The Planning Commission estimated that against the planned expenditure of Rs. 2,069 crores. domestic resources would yield Rs. 1.258 crores, leaving a gap of Rs. 811 crores. This would be met partly by external aid to the extent of Rs. 156 crores, which had already been received. There would thus be a gap of about Rs. 655 crores to be met from additional taxation, or additional borrowing or from the creation of new money. The Commission estimated that, given the retention of suitable controls over the economy, this amount of deficit-financing would not cause much trouble.

This estimate was criticised as being too optimistic. It was pointed cut that the actual amount of deficit-financing would be larger than this estimate as it was doubtful how far the different governments would be in a position to raise the planned surplus through taxation or borrowing. This criticism soon proved to be correct. The State Governments did not adopt the additional taxation measures suggested by the Planning Commission such as the levy of betterment charges etc. Thus as against the target of Rs. 413 crores fixed for the states' share of revenue in the Five-Year period, the sum actually raised is expected to be not more than Rs. 234 crorss. In the meantime, the pressure of unemployment forced the government to increase the total expenditure under the plan, which was raised to about Rs. 2,290 crores. Recent statements from the government, however, show that on account of a number of factors, the government hoped to be able to spend about Rs. 2,000 crores during the Five-Year period. In spite of this short fall, deficit-financing to the extent of over Rs. 600 crores might have to be incurred.

In the budget of 1954-55, the Central Government planned for deficit-financing to the extent of Rs. 250 crores. The Finance Minister expressed his opinion that in the next year, *i.e.*, 1955-56, the extent of deficit-finance might amount to Rs. 395 crores. As economic conditions have changed from one of inflationary pressures to that of threatened business recession and rising agricultural and industrial production, the extent of deficit-financing thus envisaged was not likely to involve any risk outside the limit of prudence.

As matters now stand, the only possible alternative to deficit-financing may be to cut down the total expenditure under the Plan, and thus to slow down the tempo of economic development. Or the government would have to force the community to accept more sacrifices. and a still further lowering of living standards in order to secure an increase in the volume of domestic savings. Of these three alternatives, economic development at planned rates through dficit-financing if necessary, or through a substantial lowering of existing living standards, or a considerably slower rate of economic development, the government has naturally chosen the first alternative. A slower rate of economic development would be of no avail in view of the large increases in population. The imposition of further sacrifices on a population living almost on the verge of starvation may not prove to be a practical proposition. Hence in spite of its dangers, deficit-financing may have to be resorted to by the government in order to secure appropriate economic development. There is, however, a need for a continuous check of economic indicators that would act as danger signals and would enable the government to take anti-inflationary measures in good time. It is a good sign that the amount of deficit-financing was cut down to a mere Rs. 500 crores in the Third Plan.

Community Development Projects : The First Plan had laid the topmost priority to agriculture. The improvements in agriculture are bound up with the progress of the rural areas. As in view of our limited resources in men and materials, it is not possible to cover all the rural areas simultaneously, it has been decided to concentrate our efforts on selected rural areas and plan for an all-round development of life of the communities living in these places. The scheme of rural development which has thus been adopted is known as the Community Development Projects.

These Community Development Projects are in essence schemes of rural reconstruction. They aim at securing an all-round development in certain selected localities. Instead of embracing a large area, the idea is to concentrate attention on a limited locality. In these localities, however, the task of improving the village life is to be tackled as a whole. The emphasis is on the simultaneous, many-sided development, each stage automatically leading to others in proper co-ordination. No single aspect of the rural life is to be neglected. A single multipurpose agency was to be set up in every village or a number of villages in these localities, and an attempt was to be made to reach the doors of every home in these areas. Last but of the greatest importance, the task of development was to be carried out, as far as possible, through the efforts of the people themselves. Instead of imposing a scheme of development upon the people, attempts are to be made to induce the people themselves to aspire for a higher standard of life and to strive for the economic betterment of the community. No lasting improvement in the village life is possible unless the villagers themselves are filled with the enthusiasm and determination to raise living conditions. Community Development Projects are based on the recognition of this vital principle.

Organisation : There are two different types of projects,—the basic projects and the composite projects. In the basic projects the emphasis throughout is on the development of agriculture and the ancilliary services. In the composite projects the emphasis is laid on the development of small industries and of a urban-cum-rural township, along with the improvement of agriculture.

Each Project will cover about 300 villages with approximately 500 square miles of area, about 1·5 lakh acres of land and 2 lakhs of population. It will approximate a sub division or a tehsil. Each project area is to be divided into 3 development Blocks, and the area of a Development Block will approximate a thana or a sub-tehsil, and each Block would cover about 100 villages. There is a provision for dividing each Block into 4 to 5 Mandi units. But for the time being the organisation of Mandi units has been omitted on account of financial stringency.

The basis of the organisation is the village unit. A village level worker or *Gram Sevak* will be appointed to look after 4 to 5 villages. These workers would be given adequate training in methods of agricul-

tural improvement, animal husbandry and other related matters of rural life. They are expected to keep in constant touch with the villages placed under their care and to encourage, and guide the villagers in carrying out the plan of development. The work of these village level workers would be supervised and guided by one Block Development Officer who would be placed in charge of every Block. Each Project will be placed in charge of a Project Executive Officer who will be responsible for carrying out the programme of community development in the Project. He will be assisted by a Project Advisory Committee which would include leaders, public workers, a few representative agriculturists, the local representatives in the Parliament and State legislatures, the Chairman of the District Board and the principal officials concerned.

There will be a District Organisation with a District Development Officer who would be advised by a District Development Board. Each State Government has to appoint a State Development Commissioner who would be responsible for directing community projects within the State. There is also to be set up a State Development Committee or a similar body consisting of the Chief Minister and the Ministers in charge of related Departments.

The Government of India has also set up a Central Committee with an Administrator of Community Projects. The Administrator is to be assisted by a highly qualified executive staff.

It has been estimated that the cost of the development plan in each project area would amount to Rs. 65 lakhs for 3 years. The Five-Year Plan has provided for a total sum of Rs. 90 crores for the period of the Plan to be spent on the Community Development Projects. A part of the expenditure would also be borne by the U.S.A. Government under an agreement signed in 1952 between the two governments. The U.S. Government would provide assistance mostly in the form of equipment and technical aid.

It is proposed to provide the village units with the following amenities :—*viz.*, at least two surface wells or tube-wells or tanks for drinking water, adequate facilities for drainage, supply of water through irrigation to at least one-half of the agricultural land, improved road system veterinary and sanitary services, schools for primary education for all school going children, primary adult education and recreation

centre etc. There are to be a veterinary hospital, a dairy and a poultry breeding centre, an agricultural school, a primary health unit consisting of 15 beds equipped for mobile work in the villages, a centre for industries, a social education and community activity centre in each Development Block.

Progress of the Community Projects : The programme during the First Five Year Plan was to bring about one-fourth of the rural population under the scheme. The plan aimed at starting work on 167 Blocks in 1952-53, and 152 Blocks in 1955-56. That a good deal of progress has been achieved must be admitted. At the end of the Second Plan, the programme was to extend to about 3100 blocks comprising about 4 lakh villages. It is expected that by October 1963 Community development work would extend over the whole country. For programmes under these schemes, the Third Plan provides for an expenditure of Rs. 400 crores. Substantial advance had been made in the execution of the agricultural programme. Over the project areas as a whole, 241,966 compost pits had been dug, 1030,573 mds. of fertilizers, 383,835 mds. of seeds, 25.075 agricultural implements of various sorts were distributed. A substantial number of wells and tanks were constructed and repaired, whereby an additional area of 310,957 acres of land were brought under irrigation. About 5827 miles of kacha roads and 303 miles of pucca roads have been constructed. There had also been considerable activity in the field of rural health and sanitation such as the construction of rural latrines, drains, sewage pits etc. More than 2,000 new schools, 5,764 adult education centres and 5,727 recreation centres had been started. As for village housing, 4.152 houses were newly constructed and 82,484 renovated. A satisfactory feature was the contribution made by the people themselves and their voluntary co-operation. Thus upto the end of September, 1960, the people contributed in cash, labour, materials etc., Rs. 93·72 crores, which was nearly 47 per cent of the total government expenditure incurred during the same period.

Criticism : But as the latest progress report on the working of the Community Projects frankly admits that while the tempo of development activity has no doubt increased, there are also large number of items in which progress of work has been markedly slow. Conspicuous examples of slow progress are to be found with regard to land reclamation programmes, rural arts and crafts etc. Secondly, in the original

budget for a Project the expenditure budgetted for in the 1st year was about Rs. 32 lakhs. But the expenditure actually incurred even in the best Project was only one-third of the prescribed amount. The actual government expenditure on all Projects inclusive of the cost of imported equipment amounted to about 36·53 per cent of the target. If the rates of expenditure do not show marked improvement in the near future, this would clearly show that the progress has not been commensurate with the expectations. Thirdly, some improvement in the training and recruitment of staff is recorded. But it has been found that in certain Community Projects, the area of operation and the population covered is so large that even the fully sanctioned staff is totally inadequate. Fourthly, Project Advisory Committees are not functioning properly and at many Projects they are non-existent. The general attitude of the members of these committees has been one of indifference and lack of interest, and where interest has been shown "it is very often of a parochial, sectional or even a personal kind which has proved more of an impediment than a help to the organisers." Lastly, there has also been some lack of co-ordination in work. One such instance is mentioned by the progress report. In many places the people have worked in large numbers to build roads. Their participation was obtained on the assurance that the roads would soon be metalled. But in a number of places, the Project Officers have not been able to carry out the promise, causing frustration and disillusionment among the people. To some extent this has been due to the formalities of government business. There has been delay in delivering the government's counterpart for the work done. Sanction has involved time-consuming formalities. At times materials or the needed staff have not arrived.

But one satisfactory feature has been the people's willingness to co-operate when properly approached. "People, especially the common people, are ready to participate to the limit of their resources in a socially worthwhile cause."

National Extension Service : Like the Community Projects, the National Extension Service (NES) has recently been started to secure co-ordinated development of rural life as a whole. The proposal to start such a service was made by the Grow-More-Food Committee (1952). That Committee recommended that there should be organised a National Extension movement covering the entire country within a period of 7 to 8 years. It also worked out the pattern of the official

and non-official organisation at all levels. These proposals were endorsed by the Planning Commission and the Government of India started the NES early in 1953. The NES was formally inaugurated all over India on the 2nd. October, 1953, a year after the introduction of the Community Projects. As a first instalment, 237 blocks were allotted for the year 1953-54. The total programme for the plan period is to undertake 1200 blocks, and it was expected that by the end of the Second Five-Year Plan the entire country would be covered by the NES.

The aim is to set up an organisation for carrying on intensive rural work which would reach every farmer and assist in the co-ordinated development of rural life as a whole. It has been modelled to some extent on the similar "extension" or "advisory" services in the U.S.A. The NES is to be the agency for carrying out the reconstruction of the villages. In the past, the government's efforts to bring about rural construction were carried out by different Departments, each working independently of one another and without a sense of common objectives. The result was that no concerted efforts were made to improve village life from all sides. No lasting improvement is possible without such a co-ordinated effort. The NES is different from these attempts. It implies a concerted and planned organisation, touching all aspects of village life, ensuring that the energies of the entire administrative machinery of the Government and of the best unofficial leadership are directed to the task of awakening mass enthusiasm.

The base of the NES is the tehsil or the taluks, consisting of about 100 to 120 villages. It would constitute a convenient development block in charge of a Development Officer or Extension Officer. He is to be assisted by a number of Technical Officers, dealing with agriculture, animal husbandry and co-operation. The organisation is to establish the closest contacts with the villagers. The lowest link in the organisation is the *Gram Sevak* or the village level workers who are to be given suitable training for this purpose. There are at present 34 centres all over the country for the training of such workers. At these centres the prospective village level workers receive training in extension methods for a period of six months in the various aspects of rural life, *viz.*. agriculture, animal husbandry, rural health, sanitation, cottage industries etc.

The estimated expenditure of a Development Block is about Rs. 7·5 lakhs for 3 years. The staff consists of one Block Development

Officer, three Extension Officers (for agriculture, animal husbandry, co-operatives and *panchayts*), two Social Education Organisers (one man and one woman), one overseer and 10 village level workers.

At each stage the utmost endeavour is to be made to associate the people with the work of development. At the village level either the *panchayat,* where it exists, or any other non-official organisation is associated for drawing up, and carrying out the plan of development. It is the task of the NES to strive to make the rural people aware of their problems and to indicate to them ways and means by which they can solve them.

By the end of 1955-56, 988 NES Blocks have been set up. The total government expenditure on these Blocks amounted to Rs. 46·02 lakhs. It is noteworthy that the voluntary contributions of the people during the same period exceeded the total government expenditure, as they amounted to Rs. 46·02 lakhs.

The results so far are on the whole encouraging, and as more experience is gained and the needed staff is well trained, there are grounds for hope that the NES will gather momentum, and will prove to be an important instrument for evolving a new pattern of social and economic life in the country side.

Achievements of the First Five-Year Plan : The Planning Commission published a review of the progress of the First Five Year Plan. This review contained an appraisal of the First Plan as a whole, and contained an account of the actual expenditure incurred on the Plan in the first four years together with a statement of the revised estimates for the last year.

The original plan provided for a total expenditure of Rs. 2069 crores, which was later increased to Rs. 2378 crores. Actual outlay over these years had been estimated to amount to Rs. 1960 crores, *i.e.*, 82% of the estimated total. The shortfall in expenditure was to be found in almost every section, though at different rates. Thus the target for investment in agriculture and irrigation was missed by only 12 p.c., as against 47 p.c. in industries and 31 p.c. in social services. As regards the timing of expenditure, the level of development expenditure was low in the first two years. It was stepped up from the third year, and the last two years accounted for almost two-thirds of the actual outlay over the five-year period. How had

the other targets laid down in the plan fulfilled ? As regards total investment, the Plan envisaged an increase of investment from a level of 5 p.c. to about 7 p.c. of the national income, the target for the aggregate investment over the five years being Rs. 3500 to Rs. 3600 crores. The actual investment, both in the public and the private sectors, was of the order of about Rs. 3100 crores in five years, and by the end of the Plan period the level of investment in the economy was about double the level in 1950-51.

As regards the growth in the national income, it increased over the Plan period by about 17·5 p.c. While the rate of increase in the national income was thus satisfactory, it has not taken place at a steady rate. There was a large increase in 1953-54 and 1954-55 as a result mainly of the increase in agricultural output. The rate of increase then diminished and was only nominal in the last year. *Per capita* incomes over the Plan recorded an increase of 10·5 p.c. It was, however, quite clear that some of the increases in the national income were rather fortuitous, especially the increase due to a rise in agricultural output.

As regards the trends in production, agricultural output showed striking improvement over the plan period. The output of foodgrains in 1955-56 at 64·9 million tons was about 3 million tons above the target laid down in the plan. The index of agricultural production was about higher by 19 p.c. The output of cotton, jute, and oilseeds also recorded substantial increases. The increase in industrial production was of the order of 40 p.c. In the production of mill cloth, the plan target was exceeded by about 400 million yards. The plan targets were also surpassed in the production of sugar, sewing machines, bicycles, paper and paper board. Cement production rose from 2·7 million tons in 1950-51 to 4·6 million tons in 1955-56, and the general engineering industries as well as heavy chemicals and chemical products recorded considerable increases. Several new products were manufactured for the first time and a number of new and important industries like petroleum refining, ship building, manufacture of aircrafts, railway wagons, penicilin, DDT etc. were estiblished. In the public sector various industrial units like the Sindri Fertiliser Factory, the Chittaranjan Locomotive Works, Telephone Industries and the Integral Coach Factory made satisfactory progress. As against this record, the projected iron and steel plant and the heavy electrical equipment plant could not be

started and the Machine Tools Factory, the Nepa Newsprint Factory and the Bihar Superphosphate Factory were behind schedule.

While the achievements of the First Plan in all these spheres had not been inconsiderable, it was in the financing that the shortfalls were most serious. In the plan as originally formulated, the amount of domestic resources to be raised by way of taxes, loans and small savings was estimated at Rs. 1258 crores. Of the balance of Rs. 811 crores, deficit-financing was to be limited to Rs. 290 crores, and external assistance was promised to the extent of Rs. 156 crores. The remainder was to be met by raising more domestic resources and or by way of external assistance. In actual practice, the amount of external assistance was only Rs. 50 crores higher than the sums promised in 1950-51. While the centre made attempts to increase its budgetary resources by levying additional taxation, the States failed altogether to raise sufficient revenues. The target of additional taxation laid down in the case of the States was Rs. 230 crores, against which they raised only Rs. 80 crores. Moreover, of the increase in revenue thus secured, a considera-able proportion was taken up by the increase in non-development expenditure and another portion was spent on schemes of development expenditure outside the plan,—so that of the fresh resources raised by taxation and the like, the amount available for the plan as such turned out to be even smaller. The result was the substantial increase in the extent of deficit-financing by Rs. 420 crores, *i.e.*, 44 p.c. higher than the plan target. The First Plan wanted to raise the proportion of tax revenue to the national income to about 10 p.c. at the end of the period. But during these five years the ratio of tax revenue to the national income increased from 7·5 p.c. in 1951-52 to only 7·9 p.c. in 1955-56.

The Planning Commission had some luck in carrying out the First Plan, in two of which the rain gods were exceptionally kind. The result of their favour had its impact on prices and the balance of payments. There was large food production and food prices started their downward trend. The wholesale index number stood at 450 in March 1951 and came down to 342·2 in June 1955, after which it started climbing up until it stood at 387 in March, 1956,—still below the level of 1950-51. The balance of payments position was extremely satisfactory due to the large increase in the domestic output of food crops. and low level of machinery and capital goods imports almost until the last year of the plan. As a consequences, the actual

drawing down of the sterling balances amounted to only Rs. 138 crores as against the plan target of Rs. 290 crores.

TABLE

Targets of production and achievement

(First Five Year Plan)

	Target of Production (5 years)	Actual Production (1955-56)	Actual as percentage of targets
1. Agriculture			
(a) Foodgrains (million tons)	7·6	10·9	143 p.c.
(b) Cotton (lakh bales)	12·6	10·3	82 p.c.
(c) Jute ,,	20·9	9·0	43 p.c.
(d) Sugar cane (lakh tons)	7·0	2·4	35 p.c.
(e) Oil-seeds ,,	4·0	5·6	156 p.c.
2. Irrigation and Power			
(i) Area irrigated (million acres)	19·7	14·0	71 p.c.
(ii) Electricity (million knot)	1 3	1·1	84 p.c.
3. Industry			
(a) Finished steel (lakh tons)	6·7	3·0	45 p.c.
(b) Pig iron	12·6	2·2	17 p.c.
(c) Cement	21·1	19·0	90 p.c.
(d) Aluminium (1004 tons.)	8·3	3·6	43 p.c.
(e) Locomotives (Nos.)	170	176	104 p.c.
(f) Mill cloth (million yds.)	982	1384	141 p.c.
(g) Handloom cloth ,,	890	639	72 p.c.
(h) Sewing machines (100 Nos.)	58 5	78·0	133 p.c.
(i) Sugar (million tons)	400	760	190 p.c.
(j) Bicycles (1000 Nos.)	433	416	96 p.c.
(k) Jue manufactures (1000 tons)	376	230	61 p.c.
(l) Power alcohol (million gallons)	13·0	5·4	41 p.c.

Questions

1. The Five Year Plan has accorded the highest priority to agriculture. How do you think this emphasis on agriculture is justified ?

2. Give a brief outline of the main features of the First Five Year Plan as prepared by the Planning Commission.

3. What are the proposals of the Planning Commission for the development of agriculture and industries in India ?

4. What sources of finance are contemplated in the Five Year Plan for the economic development of the country ?

5. What is meant by "Deficit financing" ? What role is assigned to it in the financing of the Five-Year Plan ?

6. How far do you think that the policy of deficit-financing adopted by the Government of India in implementing the First Five Year Plan is justified ?

7. Write a brief essay on (a) the Community Development Project and (b) National Extension Service.

8. What are the main features of the Community Development Projects launched in the country ? Examine their usefulness as an instrument of rural reconstruction.

9. Examine the impact of the First Five Year Plan on the volume of employment in the country.

10. Give a brief review of the progress of the First Five-Year Plan, noting its achievements and defects.

CHAPTER 45 THE SECOND FIVE YEAR PLAN

The First Five Year Plan ended in March, 1956. From the beginning it was assumed that this was to be followed by a series of plans in subsequent years with the aim of at least doubling the national income within the shortest possible time. The primary object of the First Plan was to lay the foundations on which a more diversified economy could be built up. During the Plan period both agricultural and industrial production recorded substantial increases.

It was against this background that the Second Plan was drawn up. Framed in a cheerful atmosphere, it was conceived on an ambitious scale. It provided for a total expenditure of Rs. 4800 crores in the public sector as compared to the original estimate of Rs. 2069 crores in the First Plan. The second plan had the following objectives in view :—(a) an increase in the national income by about 5 p.c. per year, (b) a large expansion of employment opportunities by about 10 to 12 million jobs in the next 5 years ; (c) rapid industrialisation with particular emphasis on the development of basic and heavy industries, and (d) the establishment of a socialistic pattern of society through reduction of inequalities in income and wealth and a more even distribution of economic power.

The total development expenditure of Rs. 4800 crores in the public sector was to be distributed as follows :—

TABLE I

(Crores of rupees)

	Second Plan Total	Per cent	*First Plan* Total	Per cent
1. Agriculture and community development ..	565	12	372	16
2. Irrigation and Flood control	458	9	395	17
3. Power	440	9	266	11
4. Industries and minerals	891	19	179	7

TABLE I—*Continued*

(*Crores of rupees*)

	Second Plan Total	Second Plan Per cent	First Plan Total	First Plan Per cent
5. Transport and communications ..	1384	29	556	24
6. Social services, housing and rehabilitation ..	946	20	547	23
7. Miscellaneous ..	116	2	41	2
	4800		2356	

(Figures relating to the First Plan have been included to facilitate comparison)

The main stress in the Second Plan was on industrialisation. Industrial and mineral development together with transport and communications claimed nearly one-half of the total expenditure as compared to about one-third in the First Plan. If power was also taken as a part of industrial development, the ratio would then rise to nearly 57 p.c. Expenditure on agriculture and irrigation which constituted 33 p.c. of the total in the first plan was to absorb only 21 p.c. in the second.

The Plan provided for an increase in agricultural production by about 18 p.c., while that of foodgrains was to rise by 15 p.c. Land brought under irrigation would increase by 21 million acres as against 17 million acres in the First Plan. The national extension and community development programmes were to cover a total population of about 325 million. The output of finished steel was expected to increase from 1·3 million tons in 1955-56 to 4·3 million tons in 1960-61 : of coal from 37 to 60 million tons; of cement from 4·8 to 10 million tons etc. Of the total expenditure of Rs. 4800 crores, Rs. 1000 crores would represent current expenditure of a developmental nature and Rs. 3800 crores represent investment, i.e., the building up of assets. In the private sector, investment was expected to be of the order of Rs. 2300 crores. Taking the public and private sectors together,—total investment would amount to Rs. 6100 crores. If, as was planned, the national

income increases by 25 p.c. over the plan period, i.e., from Rs. 10,800 crores in 1955-56 to Rs. 13,480 crores in 1960-61, the ratio of aggregate investment to the national income would then rise from its present level of 7 p.c. to 12 p.c. at the end of the Second Plan. If account was taken of the external assistance, the ratio would have to rise to at least 10 p.c., which implied a big effort on the part of the people of a poor country. The result of this rate of investment would be an increase in the *per capita* income which would rise from Rs. 280 in 1955-56 to Rs. 330 in 1960-61, —a rise by about 18 p.c. compared to 10 p.c. in the first plan period. Moreover, if the increase in the national income in the third and subsequent plan periods takes place at the rate of 25 p.c., it will be possible to double the national income by 1967-68.

The financial resources were expected to come from the following sources.

TABLE II

(Crores of rupees)

1. Surplus from current revenues at existing levels of taxation	350
2. Additional taxation	450
3. Railway contributions	150
4. Provident Funds etc.	250
5. Market loans	700
6. Small savings	500
7. External assistance	800
8. Deficit financing	1200
9. Uncovered gap	400
Total Rs.	4800

It would be obvious that the total of budgetary resources including additional taxes would bring in Rs. 1200 crores, while public borrowing would yield another Rs. 1200 crores. The problem, then, was to find out another 2.400 crores. This table was to be studied against the estimates of foreign exchange requirements of the plan. The Commission estimated that over the next five years, the balance of payments deficit would amount to Rs. 1.100 crores. This was to be financed by

drawing down the sterling balances to the extent of Rs. 200 crores. Inflow of private capital was expected to bring in another Rs. 100 crores, leaving a gap of Rs. 800 crores. This gap would have to be met from external assistance for which credit had been taken in item No. 7 (table II).

Even if external assistance to the extent hoped for was available, there would still be a gap of Rs. 1600 crores in the financial budget. The Commission considered that the government could finance its deficit by the creation of new money upto a maximum of Rs. 1200 crores. There would still be a gap of Rs. 400 crores, which was to be met somehow, either from additional taxation or borrowing or external assistance.

As had been pointed out before, the Second Plan laid special emphasis on the development of industries. If the basis for a rapid rate of industrial development in the future was to be assured, it would be necessary to make large-scale provisions for the establishment of basic and capital goods industries. The Second Plan had, therefore, more substantial provisions for the development of basic and heavy industries like iron and steel, aluminium, cement, machine tools, manufacturing of machineries etc. and a sum of Rs. 691 crores was allotted for this purpose. These industries were, by their very nature, highly capital-intensive, and so would provide comparatively a smaller volume of employment. At the same time they would lead to the creation of new income which would have to be matched by the corresponding production of consumer's goods if inflation was to be avoided. To cope with the situation, the plan proposed to adopt special measures for encouraging a faster rate of development of the cottage and small-scale industries on which Rs. 200 crores were to be spent in the plan period. Such a programme of development would make available the necessary volume of capital goods, and at the same time provide the sorely needed jobs for the people. These small industries were labour-intensive, and so would provide more employment per unit of capital than would be the case with the large-scale factory industries. Large factories producing consumer goods would be allowed to utilise their installed capacity as much as was possible. But if necessary, restrictions were to be placed on their production through various means in the interest of encouraging the development of small industries.

This is a summary of the main points of the Second Plan. It was soon felt that if the plan was to be carried out. the total expenditure would probably have to be increased by at least another Rs. 400 crores. The gravity of the food situation led to the revision of the food targets. The additional food production in the plan period was to be raised from 10 million tons to 15·5 million tons.

Criticism of the Plan : The publication of the Second Plan led to a number of controversies of which at least four were important. In the first place, critics, headed by Prof. Shenoy of the Guzarat University, were extremely critical of the financial provisions of the plan. In their opinion deficit-financing to the extent proposed would inevitably lead to inflation ; that it would not be possible to raise Rs. 450 crores through addtional taxation, neither would it be easy to gather Rs. 1200 crores through public borrowings. They regarded the plan as too ambitious and it would be necessary to cut it down in the interest of domestic stability. The second controversy related to the proposals in the plan for laying so much emphasis on the development of the cottage and small-scale industries. These industries would not be in a position to turn out consumer goods to the necessary extent, and the result would inevitably be an inflationary rise in prices. Encouraging the development of these industries would mean giving stimulus to inefficient and antiquated methods of production. It is, moreover, doubtful whether these industries would provide the expected volume of employment. Even if they did so, one should remember that the goal of economic development was not simply more employment, but the production of more wealth. Reliance on the inefficient methods of production would inevitably mean a much lower output than would have been the case if larger factories were allowed to grow.

Thirdly, the employment aspect of the Plan did not also look very encouraging. Even after an optimistic estimate, the Commission admitted that the volume of employment likely to be created during the plan period would amount to about 10 to 11 million jobs, just enough to absorb the new entrants to the labour force. Thus even after the investment of such a large sum of money, the extent of unemployment would remain at its present level. Moreover, it was doubtful whether the scheme of development would result in the creation of the estimated volume of employment. Much would depend on the cottage and small industries which were expected to provide the maximum number of jobs.

And it was here that the plan was extremely weak in structure and conception.

Lastly, as events proved later, the foreign exchange budget of the plan had not been drawn up with the care it deserved. The import contents of the various projects, *i.e.*, the volume of imports that would be needed to carry out these projects, were extremely vague and unreliable. It may not be possible to secure a considerable increase in the volume of exports as the rising incomes within the country would absorb more and more of the domestic output.

There were, therefore, three important question marks in the schemes of development proposed in the second plan. One was the big question mark relating to the adequacy of financial resources for the Plan. Would savings increase to the extent of planned investment? Or would deficit financing lead to the rise in prices? Secondly, there was the question mark regarding the availability of adequate foreign exchange resources to pay for the increased volume of imports needed for economic development. Could the amount of external assistance be raised from its present level of Rs. 200 crores to Rs. 800 or more crores? If not, how were we to secure the essential capital imports? Lastly, there was the question mark regarding the possibilities of reducing unemployment below its present high level. What would be the political, social and economic implications if, after so much hardship and tightening of the belt, there would not be any reduction in unemployment? Unless satisfactory answers were found to these questions, the Second Plan was bound to land us in considerable difficulties.

Operation of the Second Plan : The Second Plan was unlucky in meeting with heavy weather from its very beginning. The last two years of the first plan witnessed a heavy rate of investment expenditure and of deficit-financing. At the same time the monsoons were unfavourable with the result that food production did not come up to expectations. A consequence of these two facts was a rise in prices, especially food prices, which began to increase from June, 1956. The last ten months of the first plan period thus witnessed continuous rise in prices, which gathered momentum under the impact of large-scale deficit-financing in the first year of the Second Plan. As a result. the rising prices continued in the Second Plan period,—a rise brought about by the rising money incomes and the comparative inelasticity of the

food supply. The threat of inflation dogged the footsteps of the Second Plan.

In addition, the operation of the plan led to a serious foreign exchange crisis which seemed to overshadow all other problems. Large-scale imports of capital goods, both on public and private accounts, led to a rapid using up of the foreign exchange resources of the country, and as external assistance became available within a short period of time to the desired amount, a slowing or a prunning down of the plan seemed inevitable. The plan had to weather two crises,—steeply rising prices, especially food prices on the one hand and steeply falling foreign exchange assets on the other hand.

Foreign exchange crisis and the Second Plan : The First Plan was primarily a plan for the development of agriculture and irrigation. As such, it did not involve a very great draft on imports. In fact, during the first plan period the actual drawing down of the sterling balances was much less than what was planned. The Second Plan was, however, fated to be otherwise. It gave great emphasis on the development of industries, specially heavy industries, and of railways, and these schemes could not be carried out without large imports of capital goods. The balance of payments implications of the second plan were thus quite different from those of the first.

The Commission was aware of this aspect of the second plan and made some attempt to draw up a foreign exchange budget of the plan. After taking credit for the current rate of imports of capital goods, they estimated that the volume of additional imports during the plan period would amount to Rs. 1100 crores. This estimate was arrived at by calculating the volume of imports which would be needed to carry through the various projects for the development of industries and railways. To meet this gap of Rs. 1100 crores, the Commission provided for the withdrawal of Rs. 200 crores from the sterling balances. It anticipated that there would be an inflow of private capital during this period to the extent of Rs. 100 crores. The gap would thus be reduced to Rs. 800 crores which was to be met through external assistance.

This was the tentative foreign exchange budget, the most inadequately conceived portion of the second plan. Fate seemed to have played tricks with these estimates. While the Commission estimated that the amount of sterling balances would be reduced by Rs. 200

crores during the 5 years, in actual practice, Rs. 373 crores had to be withdrawn from the foreign exchange reserves within 15 months of the commencement of the second plan. Under the Reserve Bank Amendment Act of 1956, the Reserve Bank was required to keep against the note issue, a minimum reserve of foreign securities worth Rs. 400 crores, and this could be reduced under special circumstances with the permission of the Central government. In August, 1957, *i.e.*, 15 months after the commencement of the second plan, the Reserve Bank had to seek the permission of the government as its reserves of foreign securities fell below the minimum of Rs. 400 crores. It was stated that the deficit in our balance of payments had been such that the foreign assets of the Reserve Bank were declining every day by Rs. one crore, and within the next 3 months, the volume of foreign securities of the Reserve Bank would fall below Rs. 300 crores, the absolute minimum under the present Reserve Bank Act. So another act had been passed for effecting a further reduction in the amount of foreign securities to be kept against the note issue.

The reduction in the reserves of foreign securities had been due to the large deficit in the balance of payments. During the 12 months of 1956-57, there was a current account deficit of a little more than Rs. 270 crores compared to the nominal surplus of the previous year. The volume of exports remained practically at the previous year's level and was actually slightly below the level of 1955-56. Imports, on the other hand, recorded a substantial increase which was Rs. 325 crores more than the amount in 1955-56. What were the causes of this increase in the volume of imports ? This increase in the import bill was, due to increased defence needs, not anticipated at the beginning which was made in course of the year. The total value of machinery, vehicles, iron and steel and other metals rose from Rs. 299 crores in 1955-56 to Rs. 442 crores in 1956-57. A part of this increase might have been due to the under-estimation of the import requirements of the various development schemes. Some part of the increase might have also been due to the larger orders for capital goods sent by the private businessmen. These people anticipated some difficulty in getting enough foreign exchange to meet their requirements in the later periods of the second plan. To forestall such a happening they sent larger orders for the import of what they regarded as their essential requirements.

Some part of the increase in imports was also, due to increased defence needs not anticipated at the beginning of the second plan.

There were two other factors making for an increase in imports. One was a rise in the total volume of food imports whose value went up from Rs. 29 crores in 1955-56 to Rs. 102 crores in the next year. This was made necessary in order to arrest the upward movement in food prices. There was also another factor at work which was a consequence of development activities. There was no doubt that the import of consumer goods also registered some increase during these months of satisfying the higher consumption demand consequent on higher money incomes. Thus a number of factors like the under-estimation of the import contents of the development projects, the inclusion of additional projects, the build-up of stocks of capital goods by the private sector in anticipation of the shortage of foreign exchange, increased defence needs, the necessity to import foodgrains in larger amounts, and the demand for consumption goods of foreign manufacture,—combined to such a large unpremeditated increase in imports. A part of the rise in the value of imports was due to the increase in freights after the Suez crisis and the inflationry trend abroad.

Unfortunately export earnings did not increase during this year. On the other hand, the total volume of exports declined to some extent, and it was only the rise in export prices which resulted in making the total value of exports in 1956-57 almost equal to that of 1955-56. There was some evidence to show that the decline in some exports (*e.g.*, cotton textiles, sewing machines, lanterns, industrial raw materials etc.) was brought about by the pressure of domestic demand for these goods. As such, this was to be attributed increased investment activity of the second plan leading to higher money incomes and higher demand.

There was no doubt that this foreign exchange crisis was brought about primarily by the increased investment activity in the country. As such, it was invitable considering the nature and pattern of economic development proposed in the second plan. Apart from the large volume of total investment proposed to be made in the second plan, the emphasis on heavy and capital goods industries implied a shift in favour of industrial projects which required a large proportion of foreign investment goods. All these things ought to have been anticipated, at least to a greater extent than had been the case at the present instance, and adequate preparations ought to have been made in drawing up the Plan.

Instead of that the Planning Commission seemed to have acted like the celebrated Mr. Micwabar, living on the expectation that something would turn up in the nature of some external fairy to carry us through this emergency. Standby loans had been taken from the IMF., which enabled the government to have a little breathing time. The provisions regarding the reserves of foreign exchange to be kept against the note issue of the Reserve Bank had already been amended. These were mere palliatives. The whole crisis should have been tackled by promoting a large-scale export drive, and a more thorough weeding out of non-essential imports. And unless some external assistance was available within a short period, some slowing down of the plan seemed inevitable.

The scheme of priorities in the second plan : When the first plan was formulated, the country was passing through a food crisis. There was also some shortage with regard to the supply of some raw materials like jute and cotton. So the first plan gave the first priority to the development of agriculture and irrigation. About one-third of the total outlay was to be spent on schemes of irrigation and agriculture. Only 7 p.c. of the total outlay was to be on the development of industries and minerals, and its transport and communications and power development are to be regarded as forming part of industrial development, about 42 p.c. of the total expenditure was to be spent for this purpose.

As against this scheme of priority, the second plan gave a primary importance to the development of industries, on which 19 p.c. of the total expenditure was to be spent. If the expenditure on the development of power, transport and communications was included, the total came to 57 p.c. of the aggregate outlay proposed in the second plan. As aganist this, only about one-fifth of the total expenditure was earmarketd for the development of agriculture and irrigation. As regards other items, both the plans gave almost the same priority to the development of social services, housing and rehabilitation, while the allotment for the development of transport and communications was slightly increased in the second plan.

The case for the grant of a higher priority to the development of industries hardly needs to be argued in detail. Contrary to the original expectations, it was obvious that there was still some shortage in the realm of agricultural production. But main hurdle had been crossed and the bottleneck in production seemed to have been brought

under control. The increases in agricultural production and in the national income prepared the ground for a greater emphasis on industrialisation. Moreover, the need for industrialisation was also inherent in all proposals for agricultural development. No real and lasting improvement in agriculture was possible of achievement unless the surplus population was drawn away from agriculture to industries.

Thus the priority given to industrialisation in the second plan would be accepted by most people. There was, however, some difference of opinion with regard to the pattern of industrial development proposed in the second plan. According to this plan, the greatest emphasis was to be placed on the establishment of heavy and capital goods industries, simultaneously with a drive to develop cottage and small-scale industries. In this the Planners selected the Soviet pattern of development. The capital goods industries formed the foundation of the industrial structure. Industrial development cannot be secured so long as a country has to depend on others for the import of the essential machineries. In particular, the level of production of iron and steel was a major factor in determining the rate of progress for the economy as a whole. Conditions in India were especially favourable for producing iron and steel at a relatively low cost. Heavy engineering and machine industries were a natural corollary of iron and steel and provide the base for large-scale industrialisation. These industries are, however, highly capital-intensive. They require large investment of capital, but provide comparatively a smaller volume of employment. But they would add considerably to the stream of money incomes, as a result of which the demand for consumer goods would tend to increase. If the production of consumer goods is not increased at the same time, there will be a danger of an inflationary rise in prices. The additional consumer goods may be produced either in large foctories or in small-scale industrial units. But the expansion of large factories would require large investment of capital. But unfortunately we would not have much capital at our disposal after meeting the needs of the heavy industries. Moreover, the large factories would not also provide large volume of employment per unit of capital invested. Hence the Planning Commission want to go in for the development of cottage and small industries. These are labour-intensive and so require less capital, which they provide more jobs for the unemployed. It has been proposed to spend the sum of Rs. 200 crores on the expansion of these industries.

This simultaneous drive to develop heavy, capital goods industries on the one hand, and cottage and small industries on the other has been criticised by a large number of writers. This has been regarded as extremely anomalous. The capital goods industries which are to be established would turn out machines for which the only customers would be the large factories. But the plan puts the large factories in cold storage. The cottage and small industries which are to be specially encouraged will not provide the market for the former. If the large factories are to be allowed to expand fully in the third plan so as to provide a market for the machines turned out by the capital goods industries, the small industries may not find it easy to stand their competition. Penalising large factories means putting a stop to progress and growth of efficiency, and small factories mean fostering antiquated methods of production. It is also doubtful whether the small industries would be able to deliver the goods. It would, therefore, have been better if the planners provided for a smaller amount of investment on the development of heavy and capital goods industries, and earmarked a certain portion of the funds for encouraging the development of large factory industries.

Ten years of planning : The second plan ended on the 31st March, 1961, and this marked the end of ten years of planning. During these 10 years a total outlay of Rs. 11.460 crores had been incurred, consisting of Rs. 6560 crores in the public sector (Rs. 1960 crores in the first plan and Rs. 4600 crores in the second), and Rs. 4900 crores in the private sector (Rs. 1800 crores in the first plan and Rs. 3100 crores in the second). The distribution of this outlay in the public sector as between different heads of development was of course different to some extent in the two plans. Thus the first plan gave relatively greater stress on agricultural development as it devoted 31 p.c. of the total plan outlay to development programmes for agriculture and irrigation. The second plan devoted only 20 p.c. of the total outlay for this purpose. On the other hand the second plan allocated 20 p.c. of the total outlay to the development of industries and minerals as against 4 p.c. in the first plan. Both the plans earmarked an almost equal proportion of the funds to the development of transport and communications.

What have been the results of such a large outlay ? The record of growth has not been uniform. During the first plan the national

income increased by 18 p.c. as against the target of 11 p.c., mainly due to the advances made in respect of agricultural production. But during the second plan, the rise in national income amounted to only 20 p.c. as against the target of 25 p.c. As compared to the year 1950-51, national income has risen by 42 p.c. in 1960-61, while the per capita income had risen from Rs. 284 to Rs. 330 at 1960-61 prices, *i.e.*, by only 16 p.c. Agricultural production has risen by 41 p.c., while the output of foodgrains has gone up by 46 p.c. But in spite of this rise, the price level of foodgrains has risen in 1960-61 by more than 6 p.c. over the level reached in 1950-51, and it should be noted that such prices were already very high in 1950-51. The net output of organised industries has nearly doubled, and much of this increase has taken place in such key industries as steel, coal, heavy chemicals etc. A major step forward has been taken with the establishment of three new steel plants in the public sector and the expansion of the two units in the private sector. We are now producing increasing quantities of machine tools and machinery for use in agriculture and transport and for such industries as chemicals and pharmaceuticals, textiles, jute, cement, tea, sugar, etc. A large variety of electrical equipment and scientific instruments are also now being produced in the country.

While the record of progress is more or less satisfactory in many directions, there have also been a number of drawbacks. The most important was on the prices front. At the end of the first plan, the index of wholesale prices was lower by about 22 p.c. as compared to March, 1951. But by the beginning of the second plan, a distinctly upward trend in prices emerged and, at the end of the second plan, the price index had risen by 30 p.c. Food articles as a group have gone up by 27 p.c., industrial raw materials by 45 p.c., and manufactured goods by over 25 p.c. The situation was also not encouraging with respect to employment. The volume of employment no doubt increased both during the first and the second plans. But due to the large growth of population, the number of employment-seeking people was more than that of new jobs, and so at the end of the second plan the backlog of unemployment is estimated at about 9 million.

There have also been other failures. The general opinion is that the distribution of income has become more unequal during these ten years, in spite of the fact that one of the objectives of the plans was the reduction in inequalities of income and wealth. This was the result of

a number of factors such as inflation, import control, inevitable scarcities in respect of particular commodities, large-scale evasion of taxes etc. The large agriculturists, the traders and the manufacturers in organised industries have been successful in securing very large profits from rising prices, and restricted supply of imported goods etc.

Inequality of incomes generally leads to larger savings. But unfortunately the volume of domestic savings has registered a slow rate of increase during the last 10 years. Domestic savings now form about 8·5 p.c. of the national income and this is clearly inadequate. A sluggishness in the rate of growth in savings has been one of the disquieting features of the last 10 years.

There have been other mistakes or deficiencies. There have been a number of shortfalls in achievements in the agricultural sector. For example, the output of foodgrains has fallen short of the target of 80 m. tons : the cotton crop 5·1 million bales in 1960-61 was less than the target of 5·5 million bales and the jute crop of 4·0 million bales in 1960-61 was also much less than the target of 5·0 million bales. Performance was also discouraging in the irrigation sector. The net area irrigated in 1960-61 was estimated at 70 million acres as against the target of 88 million acres. There has also been a failure to ensure better utilisation of the irrigation potential newly created. There were also critical shortfalls even in respect to the "core" projects of the second plan. In coal the actual production in 1960-61 was less than the target by 5·5 million tons ; the output of finished steel was only 2·2 million tons as against the target of 4·3 million tons.

The other notable mistakes were the under-estimation of the direct foreign exchange requirements of the plan, the failure to calculate or foresee the growing import requirements of a developing economy, the failure to co-ordinate power generation programmes with industrial development programmes resulting in a power shortage, which, again, led to shortfalls in industrial production.

These are the most significant errors and failures of planning during the last 10 years. But when everything has been said on the other side, there is no denying the fact that these ten years of planning had broken new ground in every direction, stimulated industrial and economic growth and helped to strengthen the foundations of economic and social life.

CHAPTER 46 THE THIRD FIVE YEAR PLAN

The Third Five Year Plan, which had been put into operation from April, 1961, was formed on the basis of the progress achieved during the first two plans, and the perspective of development during the next 15 yars or so. Its broad aims were five in number ; viz., to secure an increase in the national income by at least 5 p.c. per annum and to provide for a rate of investment so as to secure a marked advance towards self-sustaining growth ; to achieve self-sufficiency in foodgrains and increase in the output of other crops for meeting the requirements of developing industry and exports ; to expand the basic industries like steel, fuel, power and machine building etc. nearly so that we might become self-sufficient or so with respect to them in course of the next 10 years ; to ensure a substantial expansion in employment ; and lastly, to bring about a reduction in inequalities of income and a more even distribution of economic power.

The first objective needs a little more explanation. The aim is to secure an increase in savings and investment in the economy to such an extent as would be enough to sustain the rate of growth in subsequent periods. This plan has, therefore, been characterised as a "take off" plan. To achieve this objective, the volume of investment is to be raised from 11 p.c. of the national income at the end of the Second Plan to about 14 p.c. at the end of the Third Plan. Moreover, this investment is to be designed in such a manner as to create within the country the capacity to produce the capital goods and equipment necessary to support the scale of investment proposed.

To achieve these objectives, the plan has fixed the following physical targets for the next five years. It should be noted here that the third plan makes a distinction between physical planning and financial planning. It has laid down physical targets for the different sectors of production, and the total cost of completing all these programmes of development would amount to at least Rs. 8,000 crores in the public sector and Rs. 4,100 crores in the private sector, i.e., a total expenditure of Rs. 12,100 crores. At the same time the Planning Commission have drawn out a financial plan of slightly lower amount, involving a total expenditure of Rs. 11,600 crores (Rs. 7,500 crores in the public sector

and Rs. 4,100 crores in the private sector). This has been done in view of the well-known difficulties of raising the required amount of financial resources. The details of the physical targets are given in Table I.

TABLE I

Targets of production

	1960-61	1965-66	Percentage of increase
Foodgrains	76 m. tons	100 m. tons	·32
Area irrigated	70 m. acres	90 m. acres	29
Index no. of agricultural production	135	176	30
Index No. of industrial production	194	329	70
Steel ingots	3·5 m. tons	9·2 m. tons	163
Machine tools	Rs. 5·5 crores	Rs. 30·0 crores	445
Cloth (mill-made)	5127 m. yds	5800 m. yds	13
„ (handloom)	2349 „	3500 „	49
„ (yds. per capita)	15·5 yds	17·2 yds	11
Power (installed capacity)	5·7 m.kw	12·7 m.kw	123
Railways (freight carried)	154 m. tons	245 m. tons	59

These physical targets have been fixed in view of the growth of population, growing expectations of the people and the urgent need for attaining the stage of self-sustaining growth.

Coming to financial targets, the outlay of Rs. 7,500 crores in the public sector is to be distributed as follows. (For purposes of comparison the outlays in the Second Plan have also been given side by side).

TABLE II

Distribution of total outlay in the public sector

(Rs. Crores)

	3rd Plan	2nd Plan	3rd Plan (Percentage)	2nd Plan (Percentage)
1. Agriculture and Community Development ..	1068	530	14·0	11·0
2. Major and medium irrigation ..	650	420	9·9	9·0
3. Power	1012	445	13·0	10·0
4. Village & Small industries ..	264	175	4·0	4·0
5. Industry and Minerals ..	1520	900	20·0	20·0
6. Transport & Communications ..	1486	1300	20·0	28·0
7. Social services	1300	830	17·0	18·0
8. Inventories	200	—	3·0	—
Grand Total	7500	4600	100	100

Of the total outlay of Rs. 7,500 crores in the public sector, Rs. 1,200 crores would be by way of current expenditure on social services and other developmental but recurring items, and Rs. 6,300 crores would be of the nature of new investment expenditure. The total investment expenditure would, therefore, come to Rs. 10,400 crores—Rs. 6,300 crores in the public sector, and Rs. 4,100 crores in

the private sector. The break-up of the public and the private sector investment is given in Table III.

TABLE III

Investment in the Second and the Third Plan

(Rs. crores)

Head	Second Plan Amount	Second Plan Percentage	Third Plan Amount	Third Plan Percentage
Agriculture & Community Development ..	835	12	1460	14
Irrigation ..	420	6	650	6
Power ..	485	7	1062	10
Village and Small industries ..	265	4	425	4
Organised industry & minerals ..	1545	23	2570	25
Transport & communications ..	1410	21	1736	17
Social services and miscellaneous ..	1290	19	1697	16
Inventories ..	500	8	800	8
Total ..	6750	100	10400	100

If this amount of investment is to be completed, it would be necessary to raise the proportion between national income and not investment from 11·5 p.c. at the end of the second plan to about 14 p.c. at the end of the third plan. This would involve raising the rate of domestic savings from about 8·5 p.c. at present to about 11·5 p.c. by the end

of the third plan, assuming of course that the remainder can be secured through external assistance. It is estimated that national income would go up by about 30 p.c. in the next five years from Rs. 14,500 crores at 1960-61 prices now to Rs. 19,000 crores in 1965-66. Per capita income would rise, in view of the rate of growth of population, from Rs. 330 in 1960-61 to Rs. 385 in 1965-66 at 1960-61 prices, *i.e.* by about 17 p.c.

Comments : Contrary to the Second Plan, the Third Plan has put greater emphasis on agriculture. The production of foodgrains is to be increased from 75 million tons to 100 million tons, that of oilseeds from 7·1 million tons to 9·8 million tons ; that of cotton from 5·1 million tons to 7·0 million tons etc.

The targets proposed for foodgrains would allow for consumption of about 15 ozs. of cereals and 30 ozs. of pulses per capita per day, besides providing some margin against emergencies. The target for raw cotton is expected to be sufficient to provide about 17·2 yards of cotton textile per annum per capita. The net irrigated area is proposed to be expanded to about 90 million acres. The community development programme would be extended to the entire rural area by October, 1963.

A high priority is also being given to the task of establishing a number of basic industries. The Plan provides for setting up a fourth steel plant in the public sector at Bokaro ; the production of machine tools at Bangalore is to be doubled and two additional heavy electrical projects are to be established. Near self-sufficiency is to be expected in regard to textile, sugar, cement and paper machinery. The production of cloth in the decentralised sector is to be increased from 2349 million yards to 3500 million yards ; the number of industrial estates is estimated to increase from 60 to 360.

In addition, the Plan provides for free and compulsory education for all children in the 6-11 years age-group and includes a programme of local development works for enabling all rural areas to enjoy certain minimum amenities like an adequate supply of drinking water, roads linking each village to the nearest main road or railway station, and a village school building.

The scheme of financing the plan expenditure of Rs. 7500 crores is given below.

TABLE IV

Resources for the Third Plan

1.	Balance of revenue on the basis of existing taxation	Rs.	550	crores
2.	Contribution from railways	Rs.	100	„
3.	Surplus from other public enterprises ..	Rs.	450	„
4.	Loans from public	Rs.	800	„
5.	Small savings	Rs.	600	„
6.	Provident Funds etc.	Rs.	540	„
7.	Additional taxation	Rs.	1710	„
8.	External assistance	Rs.	2200	„
9.	Deficit financing	Rs.	500	„
		Rs.	7500	„

Thus it would be necessary to levy additional taxation to the extent of Rs. 340 crores per year. This would involve increases in both direct and indirect taxes as also measures to raise the surpluses of public enterprises. The scope for increasing the rates of taxation on income is not very large and in this matter, some increase in yield may be obtained through measures to check evasion. So more recourse is to be had to indirect tax measures. The scope for deficit financing is also much less than what existed during the Second Plan. Prices are moving in the upward direction, and the cushion of sterling balances does not exist any longer. Hence the third Plan has provided for a much smaller dose of deficit-financing.

The Third Plan would naturally involve large expenditure on foreign exchange. It has estimated that the total balance of payments deficit would come to about Rs. 3200 crores, consisting of a deficit of Rs. 500 crores on account of the repayment of capital and the payment of interest, and about Rs. 2100 crores on account of the direct foreign exchange component of the Plan, plus Rs. 600 crores received on account of the PL 480 commodity assistance. As there are now no sterling balances to draw upon, the whole of this amount would have to be secured from foreign countries. Since there is no assurance

that other countries will agree to provide assistance of this order, the Plan will have to be kept flexible. The commencement and the execution of projects both in the public and the private sectors will depend on the extent to which financial assistance is forthcoming from foreign countries.

Such is the outline of the Third Plan. The pattern for the allocation of investment expenditure is almost the same as that of the Second Plan excepting that there is now greater awareness of the crucial role of the production of foodgrains and other agricultural crops. Whether the target for food production could be achieved or not would depend on the extent to which administrative lapses and inefficiencies, indecision in some vital policy matters etc. are remedied during this Plan. The resources position remains unsatisfactory. It would indeed be a very difficult task to raise additional resources to the extent of Rs. 1710 crores during the next five years as the resources have already been heavily taxed during the Second Plan period. The foreign exchange component is another uncertain and complex affair. Lastly, the position on the employment front would remain extremely unsatisfactory in spite of such a heavy rate of investment,—a rate that would strain the resources of the economy almost to the breaking point. The planned rate of investment expenditure has been estimated to provide about 14 million new jobs. But considering the large backlog of unemployment at the end of the Second Plan and the additions to the labour force during the third, the volume of new employment would only serve to increase the burden of unemployment in the economy.

It has already been noted that there is a gap between the physical and financial targets. This is intended to provide for some necessary adjustments at a later date and also for some incentives for productive enterprises. An estimate of the sources from which the necessary finance may be raised has also been revised at the same time. This is given in Table IV.

There is not much that is new in the revised proposals except that they are more optimistic with respect to the yield from existing sources of revenue and from small savings. There is no doubt that revenues from the existing taxes are increasing and would increase with higher incomes. But even after making sufficient allowance for this factor, it would rather be difficult to raise so much revenue from the current taxes also to levy additional taxes so as to bring in another Rs. 1710 crores in five years. It seems that the largest slice of this additional revenue is

to come from the indirect taxes as the rates of direct taxes are already pitched rather high. Indirect taxes lead to higher prices and are not always desirable from the welfare point of view. Collections from small savings have not been so encouraging in the last four or five years. So that one can expect still higher yields from this source alone. The price policy has not been clearly laid down, and what with higher indirect taxes and the inevitable shortages in particular lines of production, a good deal of rise in price may be fairly estimated for the future, and this is bound to create many difficulties on the wages front. It would be practically next to impossible to hold down wage rates if the cost of living index registers significant increases as a consequence of rising prices.

Financial resources * : The third plan has provided for a total outlay of Rs. 7,500 crores in the public sector. Out of this amount Rs. 6,038 crores are to be raised by the Union government, the rest being the responsibility of the state governments. How is this amount going to be raised ? A look at Table IV of this chapter will show that, apart from the surplus of current revenues (Rs. 550 crores), contributions from railways (Rs. 100 crores), market loans (Rs. 800 crores), small savings (Rs. 600 crores), main reliance is to be placed on two items for raising the additional revenues, *i.e.*, surpluses of other public enterprises (Rs. 450 crores), and additional taxation (Rs. 1710 crores). At the same time recourse to deficit financing would be of a much smaller order (Rs. 500 crores), as against Rs. 980 crores in the second plan. This is the broad outline of the sources which are expected to yield the necessary amount of revenues.

Firstly, about the usual sources of revenue, one feels that while the surplus from current revenues has been under-estimated considerably, there has been some element of over-estimation with respect to two other items, market loans and small savings. The current revenues are at present showing more buoyancy than has been taken account of in the estimates of the Planning Commission. As regards small savings it was not possible to achieve the targets during the second plan. The target was Rs. 500 crores while the actual collections are unlikely to exceed Rs. 400 crores. It is therefore difficult to accept the estimate of Rs. 600 crores from these sources. During the second plan period market loans amounted no doubt to Rs. 780 crores. But we should

* For price increased during the Third Plan, see pp. 459-462.

remember that the latter included substantial investments of the P. L. 480 funds by the State Bank of India. This item should be included in the volume of external assistance. Moreover, the Reserve Bank of India also bought a number of these securities. If these were excluded, the net investment of the public in market loans would amount to about Rs. 300 crores. To expect that this could be increased to Rs. 800 crores in the next five years appears to be a little but optimistic.

Turning to the item, surpluses from other public enterprises, the idea is that the different public enterprises like the steel mills, fertiliser factories, oil refineries, posts and telegraphs etc, should fix their rates in such a manner as to yield the sum of Rs. 450 crores in the next five years. This is also highly debatable as it is doubtful whether the various public enterprises would expand to such an extent as to bring in the required sum of revenue. Most of them are not at the profit-earning stage at the present moment, and some of them have scarcely started production. A few which have started producing have been forced to work considerably below capacity on account of a number of factors. The actual amount that could be raised from these sources is therefore uncertain.

As regards the scope for additional taxation, we should remember that quite a number of new taxes have been levied during the second plan period. It is not possible to add to the number of new direct taxes, while the rates of some of these taxes, especially the income tax, are already very high. There is of course some scope for raising the rates of income tax for the middle income groups, up to a maximum of Rs. 20,000 per year. But the amount of revenue would not be substantial. Hence greater reliance has no doubt to be placed on indirect taxation. But such taxes tend to raise the prices of the taxed goods and would affect poor and middle income groups to a larger extent than those earning higher incomes. But this has got to be tolerated when one remembers that the alternative is more deficit financing if we are to stick to the target of investment expenditure fixed in the third plan. Increased rate of deficit-financing would lead to further inflation, and that would also increase the burden on the poorer and the middle classes. One cannot but accept the proposition that "in a country like India where the bulk of the people are poor, resources on an adequate scale cannot be raised without calling for a measure of sacrifice from all classes of the people."

According to the Third Plan, the Central government was to raise an additional revenue of Rs. 1100 crores from additional taxes or from the surpluses of public utility undertakings. In the budget of 1961-62, new taxes have been levied to such extent as would yield about Rs. 450 crores during five years. In the budget of 1962-63, more taxes have been levied as would bring in another Rs. 400 crores in 4 years. So by the beginning of the second year of the Third Plan, steps have been taken to raise Rs. 850 crores out of Rs. 1100 crores. So the raising of internal resources has not proved difficult. The real trouble lies in the field of external finance.

Defence and development*: When the Third Plan estimates were published, there were doubts in the minds of many writers whether it would be possible on the part of the government to raise the additional sum of Rs. 1710 crores through additional taxation. The country, it was argued, was already taxed heavily, and so it would prove an extremely difficult task to levy more taxes. There were also great doubts whether more revenue could be obtained from all other sources as stated in the Third Plan.

When, on October 20, 1962, the Chinese attack on the frontiers of India began, the country and the government were brought face to face with a very cruel dilemma. Indian defence expenditure had no doubt increased considerably since 1950-51, it rose from Rs. 168·32 crores in 1950-51 to Rs. 366·32 crores in 1961-62. But such expenditure formed more than 40 p.c. of the total expenditure of the Union government in the former year, while the proportion had declined to less than 22 p.c. in 1961-62. We had been devoting our major attention and the major part of our resources to the task of developing the country. But the Chinese attack made it essential that we must now spend more on defence, if only to modernise the armed forces, leaving aside the question of raising the strength of the armed forces. Defence is greater than opulence and necessarily also greater than economic development. The first priority has in all cases to be given to the needs of defence. After meeting the heavily increased defence expenditure, would it be possible on the part of the government to spend the same amount of money on development? This was the dilemma. Could we maintain the same rates of expenditure as proposed in the Third Plan, while increasing our defence expenditure several times? Or

would we have to cut down the plan expenditure and slow the pace of economic development ? According to the latest budget estimates, expenditure on defence has gone up from Rs. 366·32 crores in 1961-62 to Rs. 867·23 crores in 1963-64 (including both current and capital expenditures). In other words, the defence expenditure had risen by Rs. 500 crores and if the same rate of expenditure on defence has to be continued during the remaining three years of the Third Plan, the government would have to spend an additional sum of Rs. 1600 crores on defence during the 5 years of the Third Plan. This assumes that there might be no further Chinese attack on our frontiers, and we maintain defence expenditure at the same rates as we achieved during the year 1963-64 for the remaining three years. In other words, instead of Rs. 1710 crores which we proposed to raise through additional taxation to finance the requirements of the Third Plan, we would now have to raise something like Rs. 3300/Rs. 3400 crores, *i.e.*, about double the amount originally proposed to be raised through additional taxation.

This is looking at the problem from the purely financial side. Increased defence expenditure, so far as it is spent within the country, will raise money income of the people still further. At the same time, a large part of the current production of goods would have to be diverted for the use of the armed forces, leaving a smaller net total volume of output for the civilian sector. If no steps are taken to absorb the excess money incomes, the inevitable result would be a larger dose of inflation. In other words, increased defence expenditure has got to be matched by increased savings from the people. The people must be prepared to save more, or to undergo greater sacrifices.

Are we prepared to shoulder the burden of more and more taxes and to tighten our belts still further ? Or should we cut our development expenditure to the limits of our tolerance ? But this is putting the dilemma in too extreme a form. Defence and development are not contradictory or highly competitive. On the other hand, they are to a large extent complementary. If the resources of the country are not properly developed, it may not be possible to organise the defence of the country on an efficient basis. The defence of a country on the modern scale requires a good industrial development. The country should produce still in large amounts, and should have a developed automobile industry, large number of arms factories, etc. Unless we develop our steel industry, for example, we cannot have an efficient defence organisation. The economic development of the country, with the establish-

ment of a significant industrial base is an indispensable preliminary to defence. All that is necessary is that in forming our Plan, we should now pay greater attention to the needs of defence, if we had not already done so in the past. Defence and development would have to go hand in hand. The first is not possible without the second.

If we are to pursue plans for defence and plans for development together, it would first of all, become necessary to look more closely into the various Plan schemes, and re-examine their priorities and output capacities in the light of the pressing needs of defence. Secondly, we should have to be prepared to make larger sacrifices, or to make more savings available to finance all these schemes. Of course attempts have to be made to distribute the burden of these sacrifices more equitably among the different sections of the people so that the broader shoulders of the upper income groups would have to bear greater shares of the necessary sacrifices. It may become necessary to assess more taxes on those sections of the people who, like the large agriculturists, are now escaping their share of the taxes. A more stringent attempt should be made to check evasion of the taxes by important sections of the business class, and the self-employed groups. It may even be necessary to introduce rationing in essential commodities when they are found to decline to significantly low levels. There is also scope for a scheme of compulsory savings if the government succeeds in maintaining reasonable stability in prices. In our country, at least, defence and development would have to go together. We cannot afford to have a slower rate of growth in the national income in view of the rate of growth in population and the very low levels of poverty in the country.

Progress of the Third Plan : The span of life of the Third Five-year Plan is now over. It is therefore time for us to look back, and try to assess the progress that has so far been achieved under this plan. It is well-known that our achievements under the first two Plans did not come upto expectations. The ex post positions were quite different from the ex ante ones, different in a downward direction. In course of these ten years, we did invest about Rs. 10,110 crores in the economy, of which the major part (about Rs. 5200 crores) was in the public sector, which came to an average of Rs. 1010 crores per year *i.e.*, a per capita investment of Rs. 23 per year. And the overall rise in the national income has been only 4·2%, a percentage which, as everyone knows, is much less than that achieved in many other

countries of the world most of whom have not proceeded by way of economic planning. This is not to belittle this rate of progress or achievement, for it is quite possible that our rate of growth would possibly have been much less in the absence of planning.

What have been our rates of growth during the 5 years of the third plan ? Here we should note one thing. We have started the third plan with an investment of Rs. 10,110 crores already made in the economy, with considerable reservations, extensions, and re-organisations, *i.e.*, with a more advanced base than we had at the beginning of the first 2 plans.

According to the Draft 4th Plan release, aggregate investment during the 3rd Plan period amounted to Rs. 8630 crores, which were substantially higher than the original provision of Rs. 7,500 crores. But in view of the large increase in prices, the rise in investments in physical terms had been much less than had been planned. The net results of this large investment have not of course been satisfactory. The rate of growth in the national income during the 1st four years of the 3rd Plan was 4·2 p.c., and this rate has, and should remember, been achieved in spite of bad harvests, two external aggressions and acute foreign exchange shortage. But the growth rate in per capita incomes has not been significant in view of the large growth of population, while there are a number of unsatisfactory features in several directions, such as the very large rise in prices, the failure to achieve the agricultural targets, the comparatively slower rates of growth in industrial production (7 p.c. instead of 11 p.c. as planned), the wide gap in the balance of payments etc.

What is really disturbing is that, in spite of the tremendous endeavour we seem to be making, our economy appears to exhibit all the symptoms of a stagnant economy during the first half of the third plan. It is difficult to find anything much encouraging in any of the statistics that are coming out with respect to the working of our economy.

Rising prices, rising unemployment, a comparatively slow rate of growth in industrial production and an almost stationary agricultural output and an equally stationary export trade,—all these are symptoms of stagntion in our economy. But a stagnant economy generally implies a low rate of investment expenditure. But the wonder is that we have been making quite large investments in industries, agriculture and

transport, and at the same time we are receiving very considerable foreign aid whose amount has increased in 1962-63 by Rs. 150 crores over that of 1961-62.

We must also remember that the government is also spending large sums of money on defence,—a factor which generally exercises an expansionary influence on the economy. How can one reconcile all these mutually contradictory data ? Either the economy seems to be passing through a period of pause, preliminary to a big spurt, or there is something wrong with the plan. In fact, the report of the Central Board of the Reserve Bank of India for 1962-63 was conscious of these facts when it stated at the beginning :—the year July 1962-June 1963 began in difficult circumstances with commodity prices on the upgrade, rate of industrial growth at a low point, stock marketing downward trend and foreign exchange reserves declining rather rapidly.

Plan achievements during 15 years : The Draft Fourth Five Year Plan has published some data to show the achievements of the Indian economy during the 15 year period, covering the 1st, 2nd and the 3rd Plans. While admitting that the achievements during the 3rd Plan period were unsatisfactory from many sides, it has pleaded in externation that the proper perspective should be, not the last 5 years, but the whole of the 15 years. What are the facts regarding the achievements of the Indian economy during these 15 years ?

In terms of national income data India's national income at 1960-61 prices has risen from Rs. 9,850 crores in 1950-51 to Rs. 16·630 crores in 1964-65, an increase by 69 p.c. over the period *. The compound rate of national income growth over the 14-year period was 3·6 p.c. per year,—3·4 p.c. during the 1st Plan, 4·0 p.c. during the 2nd Plan and 4·2 p.c. during 4 years of the 3rd Plan. During this period, population has grown annually by about 2·5 p.c. As a result per capita incomes have risen by 28 p.c. (from Rs. 275 to Rs. 325) over this period, *i.e.*, at an average annual rate of only 1·8 p.c.

In 1950-51, total investment in the economy was estimated at 5·50 p.c. of the national income, financed almost wholly by means of domestic savings which were also of the order of 5·50 p.c. of the national income. By the end of the 3rd Plan, the ratio of total investment to the national

* According to quick estimates, the national income for 1965-66 has declined by 3·7 p.c., over that of 1964-65.

income is expected to go up to 14 p.c., while that of the domestic savings is expected to rise by 10·5 p.c. as against 11·50 p.c. as planned earlier. This short fall in domestic savings was due to the slower rate of increase in the national income, and to the unavoidable increases in the public consumption expenditure. The result has been that our dependence on external credit has increased further during the 3rd Plan period.

Coming to sectoral details, there is no doubt that our progress in agriculture has been most unsatisfactory. But even here the annual rate of growth in agricultural production has been 3 p.c. (compound) between 1950-51 to 1964-65, as against an average rate of less than 0·5 p.c. per year in the previous five decades. The index of industrial production went up from 74 in 1951 to 192 in 1965 an increase of 159 p.c. in 14 years. Installed electric power generation has increased over fourfold from 2·3 m. kw in 1950-51 to about 10 m. kw. in 1965-66 with an additional 2 m. kw. expected to materialise during the next 12 months.

In per capita terms, the supply of foodgrains has gone up from 12·8 ounces per head per day to 15·4 ounces a day, in spite of bad weather conditions. Per capita consumption of foodstaffs has increased from 1,759 calories to 2,145 calories per day. Per capita availability of cloth has gone up from 11 metres to 15 metres. About 28 million new jobs have been created, though it is admitted, unemployment has increased during this period on account of the faster rate of growth in the numbers of working population. Other unsatisfactory features are the extremely high rate of increase in prices and the stagnation in exports.

The outline of the Draft Fourth Plan : The Fourth Plan is having a very checkered career, and though nearly 12 months of the 1st year of this Plan are gone, the final plan has not yet been given shape. The Planning Minister has submitted to the Parliament a draft of the 4th Plan in the last week of August, 1966. That Plan proposes a total outlay of Rs. 23,750 crores at 1965-66 prices, consisting of an expenditure Rs. 16,000 crores in the public sector, (*i.e.* nearly double of that of the 3rd Plan) and Rs. 7,750 crores in the private sector. This Plan has a number of special features. The experience gained during the 3rd Plan period has been taken advantage of in the formation of this Draft. In the first place, one of the prime objectives of this Draft

is the increasing emphasis it has placed on self-reliance and discontinuance of foreign aid. Thus agriculture has been given the highest priority which covers not only the programmes of agricultural production but also such industries like fertilizers, pesticides and agricultural implements. In the agricultural sector the anticipated production by 1970-71 includes 120 m. tonnes of foodgrains, 13·5 m. tonnes of sugarcane, 10·7 m. tonnes of oilseeds, 8·6 m. bales of raw jute, etc. The realisation of those estimates would result in a compound rate of growth of 5·59 p.c. per annum in agricultural production—5·92 p.c. in the case of foodgrains and 5·01 p.c. in the case of non-foodgrains. The total outlay in the 4th Plan under agriculture and allied programme will be around Rs. 2,400 crores in the public sector, and Rs. 900 crores in the private sector. The total provision for minor irrigation works under different heads is double of that in the 3rd Plan. The country is expected to be self-sufficient in food by 1971 in spite of the increased population and increased provision for food for everybody. The PL. 480 imports of food over the 5-year period is expected to be restricted to only 19 m. tons.

Secondly, special emphasis has been laid on price stability and for this purpose the Draft Plan document provides that there shall be no recourse to deficit-financing at any level during these 5 years. Detailed indications have been given in the document, unlike the previous plans, from where the additional resources of Rs. 1000 crores are to be raised. The utmost economy is to be exercised with respect to non-Plan expenditure, which should not be allowed to exceed by more than 5 p.c. per year, and should be normally restricted to 3½ p.c. per year. Another important point in the connection relates to wages and salaries. It is pointed out that apart from some minor adjustments in wages and salaries at the lower levels, there must not be any general increase in the wages and salary structure either in the public or the private sector. At the same time, the government must assume responsibility to maintain the prices of essential commodities at reasonable levels, by undertaking, if necessary, wholesale and retail trade of some basic articles of mass consumption.

Another sector to receive top priority is family planning for the purpose of reduction in the birth rate from 40 per 1000 population to 25. The Plan has allotted a sum of Rs. 95 crores to family planning in the first instance, and has further provided that when this programme

is completed, consideration will be given to provide the Family Planning Department with an additional outlay of Rs. 144 crores,—the only solitary instance in the whole document where provisions for additional outlay have been made.

It is time for us to turn to the specific details of the Draft Plan. The following table given the sector-wise allocations made in the Plan, and the outlays incurred on these accounts in the 3rd Plan are given side by side for purposes of comparison.

TABLE I

(In crores of rupees)

Head of Development	Outlay in the 3rd Plan	Outlay in the Draft 4th Plan
Agriculture, Community Development & Co-operation	432	2410
Irrigation	44	964
Power	260	2030
Village & Small Industries ..	171	370
Organised Industries & Mining ..	3751	3936
Transport & Communication ..	2575	3010
Education	323	1210
Scientific Research	190	140
Health	164	492
Family Planning	86	95
Water Supply	3	373
Housing & Construction	140	280
Welfare of backward classes ..	90	150
Social Welfare	30	50
Craftsman training & labour welfare ..	85	145
Public Co-operation	7	10
Rural Works	95	95
Hill areas & Special areas	6	50
Rehabilitation	90	90
Other Programmes	44	70
Grand Total ..	8536	16,000

Of the total private sector outlay of Rs. 7,750 crores, Rs. 2350 crores will be on organised industries and mining, Rs. 1500 crores on water supply, Rs. 900 crores on agriculture, Rs. 630 crores on Transport & Communications, Rs. 320 crores on village and small industries, Rs. 50 crores on irrigation and Rs. 1900 crores on other programmes.

To enable the public sector to incur an outlay of Rs. 16,000 crores, the following financial resources are expected to be raised during the 4th Plan period.

TABLE II

(in crores of rupees)

Heads of revenue	3rd Plan	4th Plan
Balance from current revenues at pre-Plan tax rates	470	3016
Cntribution of railways on pre-Plan basis ..	80	266
Surplus of other public undertakings ..	395	1085
Loans from public (net)	915	1500
Small Savings	585	1000
Unfunded debt (net)	340	565
Compulsory deposit & annuity deposit (net)	115	150
Miscellaneous capital receipts ..	185	665
Budgetary receipts (external credits)		
(*a*) Other than PL 480	1575	4340*
(*b*) PL 480	880	360*
Economies in non-Plan expenditures ..	—	335
Additional mobilisation of domestic resources	2,880	2730
Deficit-financing	1,150	—
Aggregate resources	8630	16,000

* at post-devaluation ratios.

To raise additional domestic resources, the Draft proposes an increase in the rates of land revenue, higher irrigation rates, a surcharge on commercial crops, higher electricity rates, additional taxation on property and wealth, adjustments in direct and indirect taxes etc. There is to be recourse to deficit-financing under any circumstances.

The gross external credit requirements for carrying out the plan projects, excluding PL 480 inflows have been estimated to be 8·4 billion dollars. This includes debt repayments amounting to 1·7 billion dollars

and private net investment of 0·9 billion dollars. Excluding these from the total, we are left with 5·8 billion dollars or Rs. 4,340 crores at the post-devaluation rates, and this has been assumed in the estimates of financial resources. According to the Draft, foreign exchange required for debt-servicing as well as for maintenance imports should be met from increased export earnings during the 5th Plan period. In other words, the economy is expected to achieve self-sufficiency by the beginning of the Sixth Plan.

Outlays of these amounts, it is expected, will raise farm production at the compound rate of growth of 5·59% per annum. Efforts will be made to step up food production to 120 m. tons by the end of this Plan. There will be more than three fold increase in the production of fertilisers, and doubling of the programme under soil conservation and improved seeds. A new strategy based on an intensive area development approach and high yielding fertiliser responsive varieties will be adopted. The programme also gives the highest priority to industries manufacturing industrial inputs for agricultural such as fertilisers, pesticides, farm equipment etc., metals and machine-building industries including steel, aluminium, zinc etc., intermediate products industries such as industrial chemcals, petroleum, coal, and also industries producing essential consumer goods such as sugar, cloth and kerosene etc.

This is the main outline of the Draft Fourth Plan. There is no doubt that many will regard it as another over-ambitious, especially in view of the short-falls in the achievements of the Third Plan. That Plan had involved the nation in tremendous efforts and sacrifices. But the results have not been satisfactory. There are grave doubts whether, over and above the burdens imposed during the 3rd Plan, the country will be in a position to raise such large resources as would be needed to carry through a Plan of this size. A big question mark also hangs over the availability of so much external credit. So far as the present expectations go, so much external credit as has been assumed in the Draft Plan is extremely unlikely to be available, unless there takes place a fundamental change in the policies of the donor governments. What possibility then exists for the completion of a plan of this nature in view of the extremely limited domestic and foreign resources ? The draft Plan has no doubt made some re-thinking about agricultural production. But here also one notes with some skepticism the fact that while the Plan programmes have not always been based on the basic

needs of the agricultural situation, the machineries for the implementation of such imperfect programmes have often fallen far short of the requirements. This Draft does not seem to mark any exception from the usual trends. The price policy will have to be framed more seriously than we have as yet witnessed. Another round of price increase by 30 p.c. during this Plan also will certainly spell disaster. The employment situation will also be no better after this Plan than it had been after the last 2 Plans.

On the whole the draft leaves many hostages to the fortune, fair weather and foreign friends. One is of course conscious of the force of the argument that a smaller plan will imply a very slow, and an almost pedestrian pace of growth in view of the large increases in population. But one is not so easily convinced that this imperative forces the country to have Plan of a size for which it may be extremely difficult to raise enough resources.

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